CITY OF KIRKLAND
Department of Finance & Administration
123 Fifth Avenue, Kirkland, WA 98033 425.587.3001
www.ci.kirkland.wa.us

MEMORANDUM

To: Dave Ramsay, City Manager

From: Tracey Dunlap, Director of Finance and Administration

Date: February 20, 2007

Subject: Consolidated Summary of Phase 1 Fiscal Analysis

In preparation for the March 1, 2007 Public Forum, we have compiled the final results of the Phase 1 fiscal analysis as requested. Please find included the following documents:

- Annexation Fiscal Analysis Memo
  12/12/06 Council Meeting
- Attachment A: *Final Summary of Findings*–Updated February 2007
- Annexation Fiscal Analysis–Study Session #2
  1/9/07 Council Study Session

The documents listed above will be posted to the Annexation website under "Annexation–Important Information." An email will be sent out to the annexation listserv with a link to the consolidated report. A hard copy of the report will be mailed to those who attended the previous forums and who do not have an email contact.

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MEMORANDUM

To: David Ramsay, City Manager

From: Tracey Dunlap, Director of Finance and Administration

Date: December 4, 2006

Subject: Annexation Fiscal Analysis

RECOMMENDATION:

Council receive the preliminary draft findings of the Annexation Fiscal Model and an introduction to the policy framework.

BACKGROUND DISCUSSION:

Introduction

In September, the City engaged Berk & Associates to create an analytical model to project the long-term fiscal impacts of annexation under a variety of different development, cost, and revenue scenarios and to assist the City in identifying strategies to address the projected financial shortfall from annexation. The information developed for the 2005 annexation analysis forms the basic starting point for this effort, but the model also merges the City of Kirkland financial forecast projections with the Potential Annexation Area (PAA) to provide a full picture of the impacts. The model also addresses the potential benefit provided by the sales tax credit made available by the Washington State legislature to aid in annexation transition for up to a ten year period. An overview of the key concepts and policy options in the model was presented to the City Council on November 8.

Attachment A contains the draft summary of findings prepared by Berk & Associates, which describes the fiscal model and discusses the key assumptions, policy choices, and preliminary draft results.

Why are we looking at annexation now?

In 2005, the City evaluated the potential annexation and determined that the fiscal deficit projected at that time was a substantial obstacle to annexation. In the meantime, the Washington State Legislature enacted a sales tax credit funding mechanism to encourage annexation. To qualify for this ten year sales tax credit, the annexation must commence by 2010. The magnitude of the sales tax credit warranted revisiting and refinement of the annexation analysis to determine if it sufficiently mitigated concerns related to the fiscal deficit.

How does this evaluation differ from previous annexation studies, especially the work completed in 2005?

The 2005 work involved estimating the incremental budget impacts of serving the PAA and estimated the annual operating cost and revenues. The current fiscal analysis looks at the potential annexation area (PAA) over the 2010-2025 time period, as well as the City's overall financial condition for the same period of time. The fiscal study combines the work done in 2005 with a detailed financial projection over time for the entire City, with or without annexation. The importance of analyzing the PAA within the context of the overall City budget lies in the interrelationship between the two. The measures that the City Council takes to address the fiscal deficit in the PAA impact the City as a whole and vice versa. As a result, a review of the City's current financial forecast is a necessary first step.

What is the City's current fiscal forecast?

The City's financial forecast demonstrates an existing structural imbalance between revenues and expenditures. The financial forecast for the current Kirkland boundaries has not fundamentally changed from that presented as part of the budget process over the years because the City's financial position has not fundamentally changed. Like most local governments, expenditures are increasing faster than revenues. Like most other local governments the deficit is addressed incrementally – one year at a time (or two years in the biennial budget) because the City Council is required to pass a balanced budget each year. The City's fiscal policies call for ongoing revenues to match ongoing expenditures in the budget. Each budget period, the City Council approves a balanced budget by taking a variety of actions that are appropriate at that time that mitigate the factors causing the structural imbalance that exists in the tax-supported services and to address service level needs identified at that time. The table on the following page summarizes the actions that Council took to balance the budget over the past five to ten years.

The causes of Kirkland's structural imbalance are largely the same as for most local governments. The combined effects of a stalled economy beginning in 2002 with voter-approved initiatives that eliminated some revenue sources and limited others created a "one-two punch" to Kirkland's otherwise stable and diversified revenue base. On the other side of the ledger, increases in health care costs and cost of living adjustments have resulted in growth in employee costs beyond normal inflation. Employee costs account for nearly 70% of General Fund expenditures. At the same time, citizen expectations for services have not wavered. Council has recognized the need for additional staffing in critical areas, such as public safety and development services, but recent budget processes have necessarily focused on maintenance of existing services. Over the years, the Council has made expenditure (and service level) reductions, raised taxes, and benefited from economic growth in order to balance the budget. The financial forecast provides a useful perspective on the City's financial future, however, its accuracy fades past the first few years. The forecast demonstrates the City's future constraints, but does not dictate future actions. Each budget cycle, the City Council must take actions that are appropriate for that time, taking into consideration factors that changed from the prior forecasts (e.g. voter initiatives, economic downturns or upturns, changes in the retail business base, etc.).

Strategy	< 1999	1999	2000	2001	2002	2003	2004	2005-06
New revenue source:								
Surface water management fee	X							X
Revenue generating regulatory license fee						X		
Surface water utility tax					X			
Cost of service interfund charge	X							
Increased tax rate or fee:								
Increased property tax rate	X		X			X	X	X
Increased utility tax rate						X		X
Increased parking fines			X		X			
Increased development fees		X	X		X			
Changes to sales tax:								
Reduced CIP allocation			X					
Reduced sales tax lag to 1 year								X
Used one-time revenue source:								
Sales tax audit proceeds							X	
Interest income								X
Planned use of Rainy Day reserve						X	X	X
Expenditure reductions					X	X	X	
Other strategies:								
Used new construction growth	X	X						
Reduced budgeted benefit rate to citywide average					X			X
Reduction in state retirement rates					X			

Does annexation make the City's fiscal forecast better or worse?

Initial modeling confirms that "closing the gap" is not likely to be accomplished by any single change in development strategy, cost structure, or revenue base but rather through a combination of changes to all three elements.

In the near term (and without the State sales tax credit), annexation increases the City's fiscal gap primarily due to the facilities needs required to provide services in the PAA. However, with the sales tax credit, the gap in the PAA can be narrowed or eliminated through strategic financial management, the combined City and PAA "gap" is not as large as the current City gap over time. In other words, if the City can maximize the sales tax credit, it helps to address the PAA gap in the first ten years after annexation and the PAA helps reduce the future deficit of the City. During the same ten-year period when the state sales tax revenue is available, the City will be faced with a series of decisions to address its own structural gap. Therefore, the impact of annexation has to be viewed from the perspective of whether the addition of the

PAA will improve the impact of those decisions as they occur. To test this dynamic, a number of different policy scenarios have been generated to assess the impact of different actions.

Not surprisingly, the near-term gap grows from annexation, although much of this increase is mitigated by the State sales tax credit during the first ten years. However, in the latter years, nearly any action the City Council takes to close the City's projected financial gap will close the annexation gap and result in a more positive overall outcome. This occurs because the City benefits from having a larger population, employment, and tax base, which should provide some economies when applying the measures required to address the current City's projected gap. In addition, the level of new development activity in the PAA is expected to increase during the latter years of the forecast period, recognizing that the City's current land supply will begin to reach build-out during the projection period. As described in Attachment A, the impact of the policy choices improves after annexation in the long-term.

Why is this different from the results of the prior evaluations?

This study approached evaluating the impacts in a manner that differed from prior studies:

- It is important to recognize that the projected annexation figures will continue to change over time based on refinements in estimates. For example, the $4.8 million funding gap in the PAA estimated in the 2005 evaluation was reassessed in early 2006 and had closed somewhat due to Council action related to public safety staffing at year-end 2005 and improvements in economic conditions.
- The analysis looked at the needs of the City as a whole over time, rather than isolating only the impacts of annexation at a point in time.
- By looking at the whole City, the estimated resource needs for public safety purposes could be reduced by recognizing that there could be some economies realized by looking at patrol districts across the current City boundaries. One of the underlying assumptions in the 2005 analysis was that the needs of the PAA should be addressed as a stand alone service area. As a result of these changes, the fiscal gap was reduced by approximately $1.8 million.[1]
- Current planning for facilities needs indicates that, if annexation does not occur, a new Public Safety building would not be necessary, with the total needs for expansion of City Hall and the Maintenance Center projected at $30 million. If annexation occurs, the current estimate for a new Public Safety facility is $44 million (reflecting a 75 bed jail), resulting in total facilities expansion costs of $80 million (which also reflects the additional City Hall/Maintenance Center space needs for additional annexation staffing). The impact of the increased needs is allocated to the PAA in a manner that reflects the proportional share of the incremental needs (this issue is discussed in more detail in Attachment A).

What are the policy choices to consider related to closing the gap?

Attachment A contains a detailed discussion of the policy choices available to address the fiscal gap, which involve the application of some or all of the following tools:

[1] Note that the possible need to add fire personnel in the Kingsgate area, should the decision be made to relocate Fire Station #34, is not reflected in the current annexation cost projections since discussions are on-going related to options for ensuring coverage for this area. This issue is discussed further at the end of this document.

1. Development-related revenue
   - new construction property tax
   - sales tax

2. Tax policy revenue
   - property tax
   - utility tax
   - business tax

3. Expenditure management
   - level of service – staffing levels
   - efficiency/productivity
   - compensation

In the scenarios reflecting a variety of policy choices tested to date, potential actions taken to address the current City's gap are improved with the addition of the PAA. It is important to note that this evaluation has been undertaken to evaluate the financial impact that annexation will have on the City over time, not to decide on a course of action to close the City's fiscal gap over the next 20 years. Those decisions will be made over time as each budget is balanced, recognizing the economic conditions, service needs, and policy choices of this and future City Councils.

What are some of the major financial issues to be evaluated in Phase II, if the decision is made to proceed?

- The analysis assumes that Kirkland will receive the maximum state sales tax credit for the ten-year period and that the funding will remain intact for the whole timeframe (meaning there will be no reductions in the funding level contemplated in the legislation). In addition, the method for demonstrating eligibility for the full credit is still under development and negotiation with the state.
- The infrastructure needs of the PAA will be evaluated as part of Phase II. The fiscal study addressed facilities needs and projected revenues that would be available to fund infrastructure improvements, but the actual infrastructure requirements will need to be identified based on a technical assessment of the deficiencies in each area.
- The availability of funds from King County to assist with the annexation transition would be negotiated as part of Phase II.
- The impacts of adding fire staffing to meet the needs of the area currently served by the Kingsgate station in the event that the station is relocated are not reflected in the draft analysis. The magnitude of the requirement is dependent on when and where a new station would be located and the City's ability to negotiate for coverage with neighboring agencies.
- The ultimate sizing and configuration of the new Public Safety/Jail facilities required with annexation is currently under study as a separate effort expected to be completed in the next few months. The facilities financing and impacts of annexation would be impacted by alternate public safety facility scenarios.
- The Northshore Utility District provides water and sewer services in most of the PAA. The City and the District currently have a franchise agreement which includes a time limited non-assumption clause. At this juncture, the analysis assumes that the District will continue to provide these utility services, but also assumes that the franchise fee charged to the District will keep pace with the utility tax rate applied by the City to its own utilities.

Conclusion

The presentation on December 12 will include an overview of the preliminary findings and discussion of the policy framework established for evaluating fiscal scenarios.

CITY OF KIRKLAND
LONG-TERM FISCAL IMPACTS OF ANNEXATIONS

Final Summary of Findings

February 2007

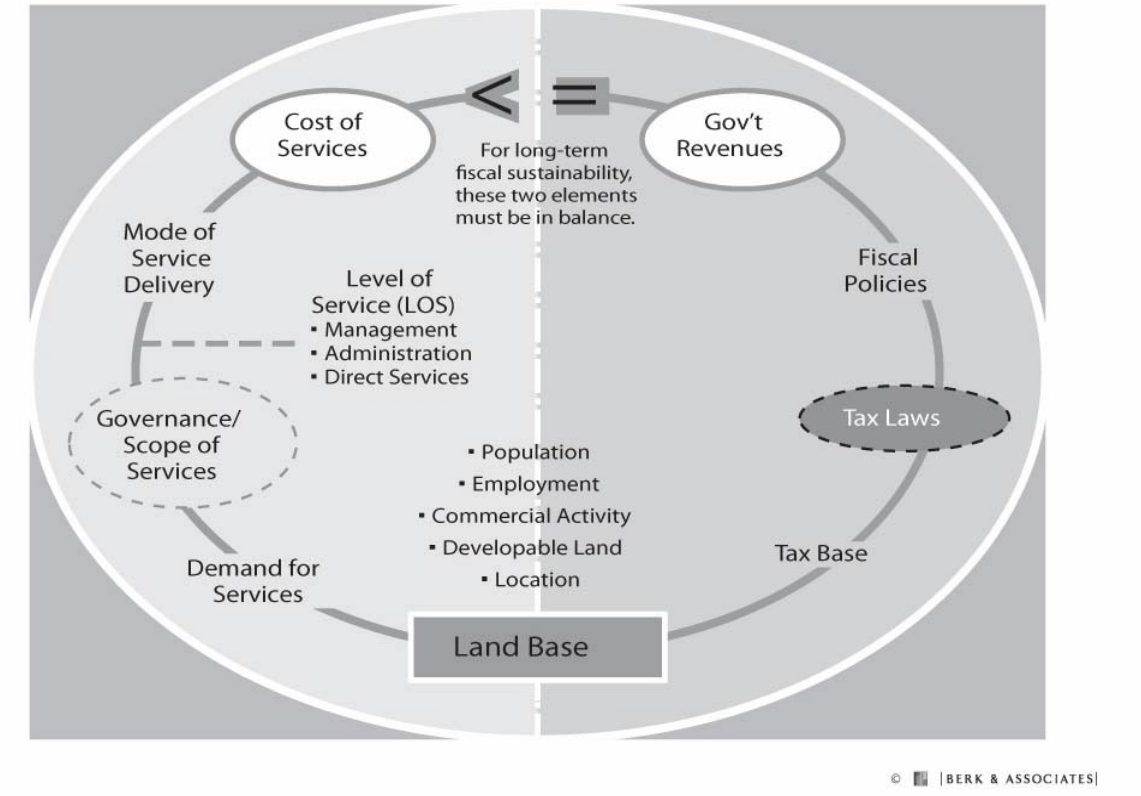
PURPOSE AND OBJECTIVES OF MODEL

- The model is designed to estimate revenues and expenses for the current City of Kirkland as well as post-annexation versions of the city.
- While the model is not Fund-based it does isolate the components of the City's budget that are funded through general tax and fee revenues, including functions and departments within the General Fund, Street Operating Fund, Parks Maintenance Fund, Facilities Maintenance Fund, Equipment Rental Fund, and Information Technology Fund. The model does not include the utility enterprise funds, since they are not tax-supported.
- Capital cost implications are included only for the equipment, fleet and facility costs associated with increasing staff levels associated with growth or annexation. Capital implications related to new public infrastructure are excluded from the model.
- While infrastructure costs are excluded, the model does estimate future capital-restricted revenues (such as gas tax distributions from the State and real estate excise tax) for the current City and the PAA's.
- Another objective of the model is to factor in the new sales tax credit funding enacted by the State Legislature.
    - This funding is designed to assist eligible cities that annex by 2010 by providing support for up to 10 years. Therefore, the model runs through 2025, five years past the last possible year of sales tax credit funding support.
    - The model estimates the maximum sales tax credit and the eligible annexation deficit to determine the amount of potential revenue from this source.
- The model has built-in flexibility that will allow city staff to support policy discussions related to fiscal issues pre- and post-annexation.
- This flexibility is derived from the model's ability to show the impacts of a variety of scenarios. City staff can vary the following:
    - Development scenarios;
    - Tax policies;
    - Cost of services including level-of-service; and
    - Annexation transition assumptions, such as the possibility of phasing in the impact over several years.

CONCEPTUAL MODEL FRAMEWORK

- The model was developed using a conceptual Fiscal Balance Framework, which operates as follows:
  - Factors in the land base, such as population, employment, and commercial activity, drive both demand for services and the tax base.
  - Depending on a jurisdiction's scope of services and choices regarding level of service, demand for services leads to costs.
  - Depending on a jurisdiction's choices regarding fiscal and taxing policy (limited by tax laws), its tax base will lead to tax and fee revenues.

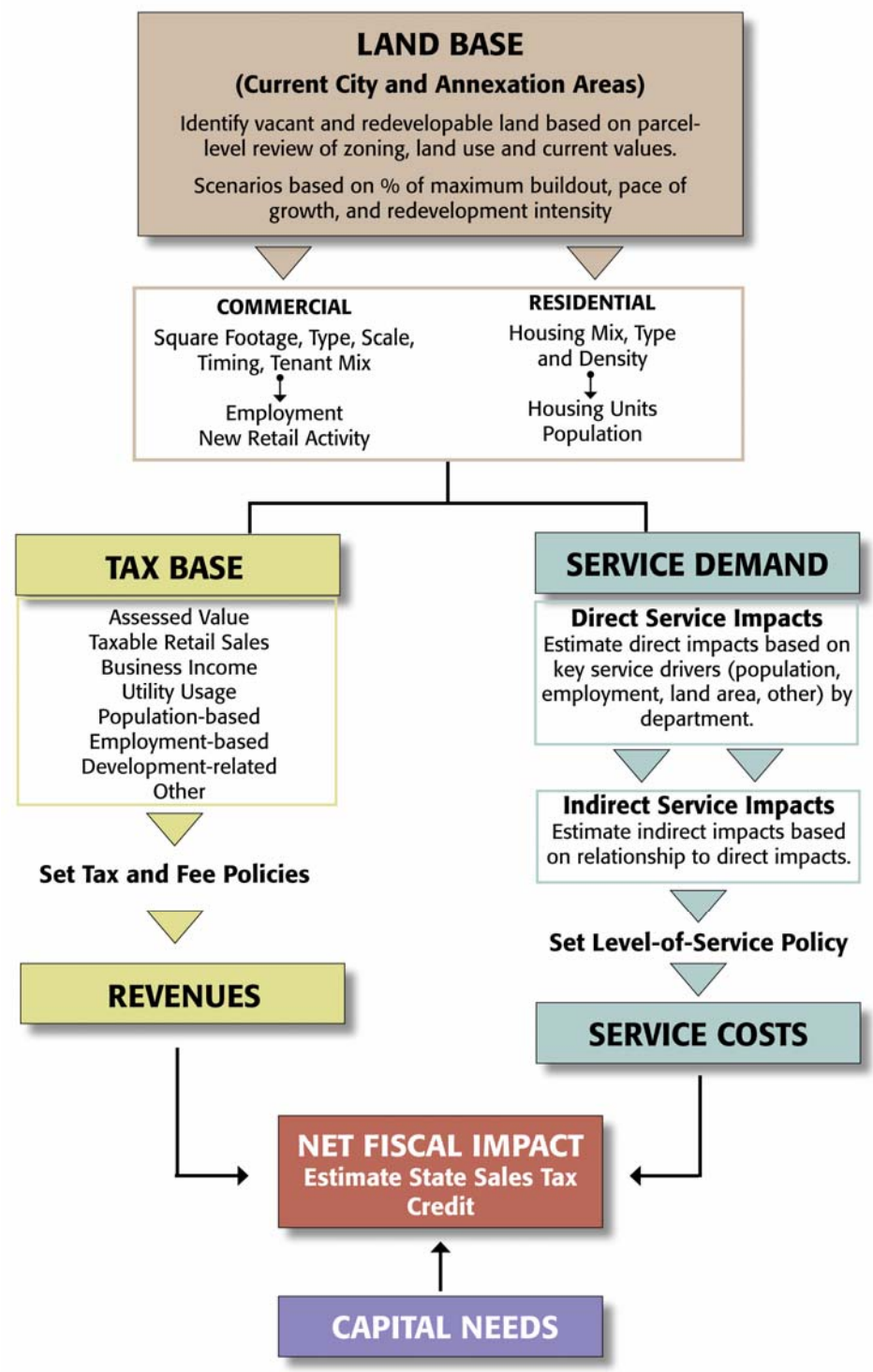
Fiscal Balance Framework



- A particular challenge for this project is the need to project land base changes over a 20-year window.

MODEL SCHEMATIC

Long-Term Fiscal Model Schematic



MODEL FLEXIBILITY TO SUPPORT POLICY ANALYSIS OF ANNEXATION

Three Elements Will Dictate Kirkland's Long-Term Fiscal Balance

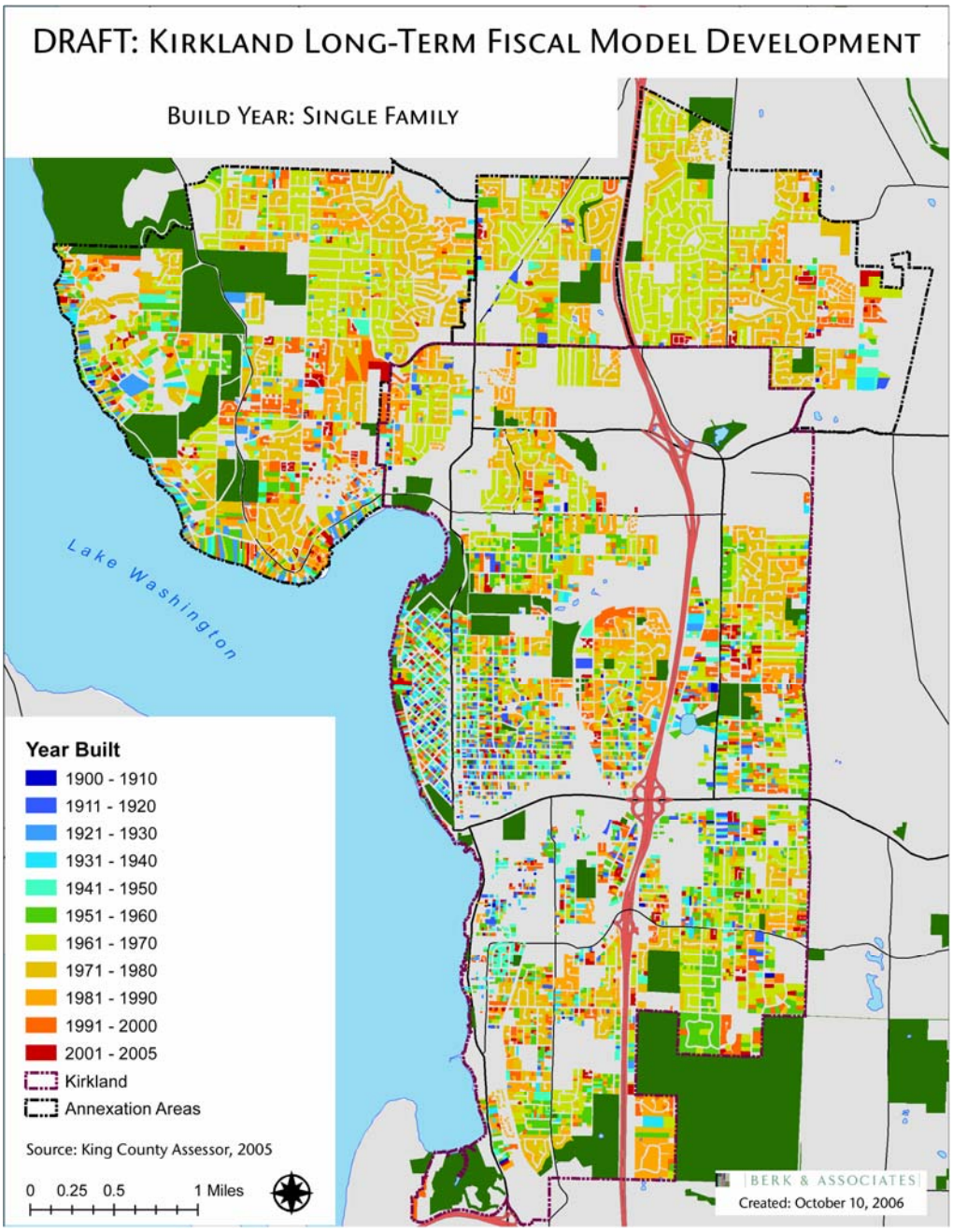
- Balancing future budgets for the City (regardless of annexation) will depend on one or more of the following:
    - **Development.** While the City does not directly control the pace, scale or type of development activity, this will have an impact on future costs and revenues. Varying development scenarios for single family, multifamily, and commercial/industrial properties allows for the risk assessments and testing the effects of other city policies designed to affect fiscal balance.
    - **Cost factors and level of service changes.** As development and/or annexation occur, there will be increases in demands for services. The City will be making choices about the level-of-service provided.
    - **Tax policy changes.** The other major policy variable for the City to consider in balancing its budget is the tax policy, including taxes on property, businesses, and utilities.
- It is important to note that these are the factors that are in play every time the Council considers its next City budget. The question is the same – "how do we balance the budget?" – and the choices are the same – "can we afford to maintain current levels-of-service?" and "do we need to consider changes in tax policy to fund essential city services?".
- Since this is a long-term financial planning effort, the Council will need to grapple with these issues in a somewhat more conceptual way. The immediate task is not about making specific decisions or plans to balance future budgets, but rather to identify how annexation might affect the City's ability to meet these fiscal challenges in the future.

DEVELOPMENT SCENARIOS

- Both revenues and costs will be dependent on the type and quantity of development over the next 20 years. As a result, it is important to have the ability to test different development scenarios in order to evaluate the fiscal implications of growth on the City and how different growth trends affect the City's fiscal and annexation policy choices.
- The development model is based on zoning and land use information for all 22,000+ parcels in the City and PAA's, under current zoning unless otherwise noted. The parcel module is where assumptions can be varied to create alternative "maximum development" scenarios.
- Within the fiscal model one chooses from the list of "maximum development" scenarios and then select what percent of the max will be achieved by 2025 and whether the development will be front-loaded (with a user defined share occurring within the first 8 years), back-loaded (with a user defined share occurring within the last 8 years) or occur in a relatively linear fashion.
- The model has several maximum development scenarios, each based on the current zoning in the City and PAA's. The differences are in the settings for redevelopment (low, medium and high redevelopment scenarios) and the degree to which some environmental factors (such as steep slopes) may reduce the development capacity.
- As an illustration of the maximum development concept, the following maps show the components of the development potential, with a particular focus on the single family housing component. The maps include:
    - Build Year. Shows how the average age of single family homes and how this may relate to the potential for redevelopment and reinvestment throughout the City and PAA's
    - Land Value. Show the distribution of land values throughout based on current County Assessor assessed value of land.
    - Improvement to Land Ratio. An indicator of redevelopment potential which identifies the ratio of improvement value to land value. A ratio of less than 1.0 suggests that the land is worth more than the building.
    - SF (Vacant, Subdividable, Redevelopable). Shows the single family parcels that are shown to be currently vacant, subdividable or redevelopable. The subdividable properties must be at least 2 times larger than the minimum lot size for the parcel. Redevelopable properties are shown at two different redevelopment thresholds: improvement to land ratio of 0.25 (building less than 25% of land value) and a ratio of 0.5 (building value less than 50% of land value, but more than 25%). As a point of comparison, the city's Planning Department uses 0.5 as the threshold for likely redevelopment.
    - Potential for new and redeveloped Multi-Family Units. This map shows the distribution of potential new multi-family units.
    - Potential for new and redeveloped Commercial/Industrial Square Footage. This map shows the distribution of potential commercial and industrial space.

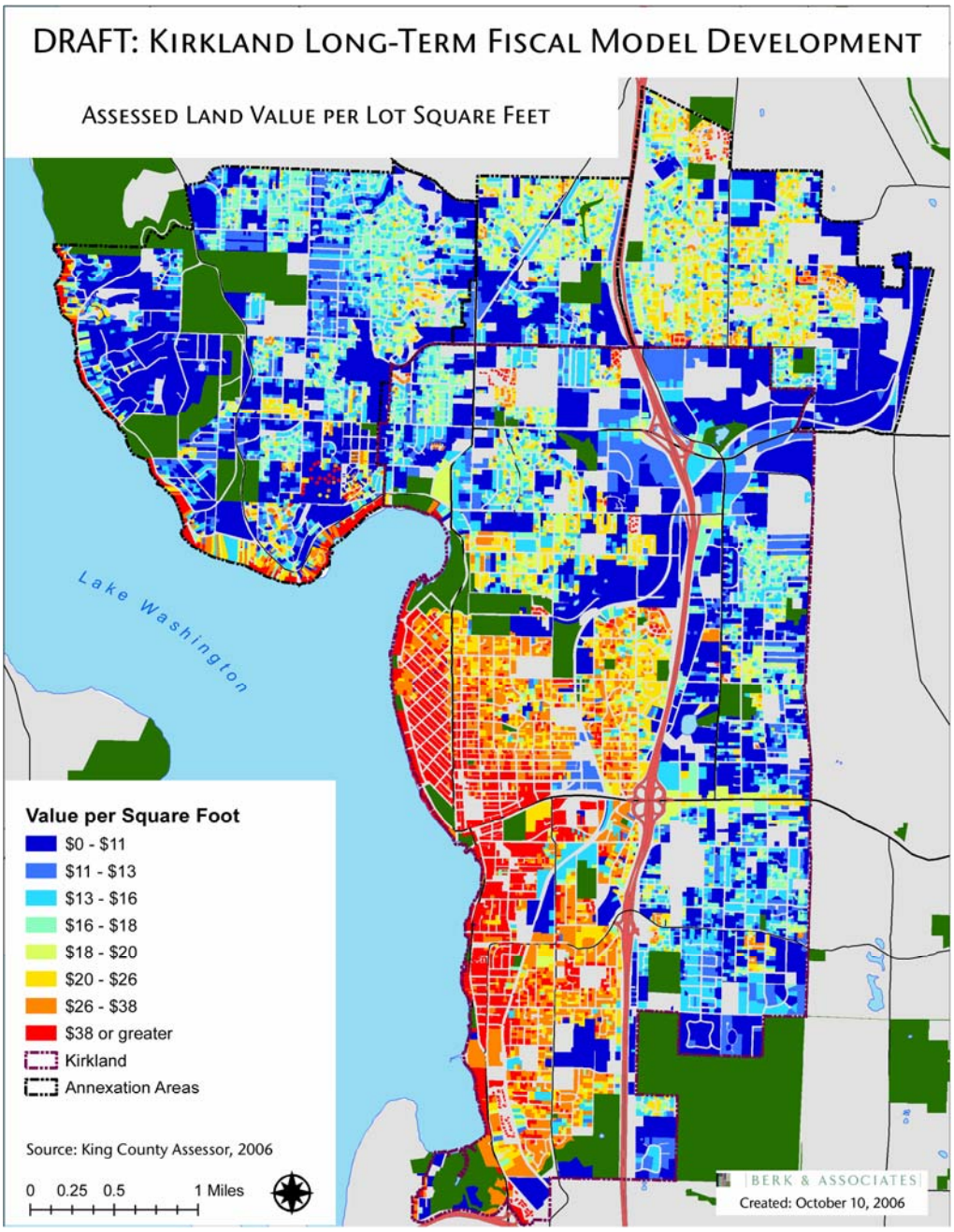
BUILD YEAR

- Older single family homes are scattered throughout the City and to a less degree the PAA's, but are clearly focused in the area immediately north of downtown Kirkland.



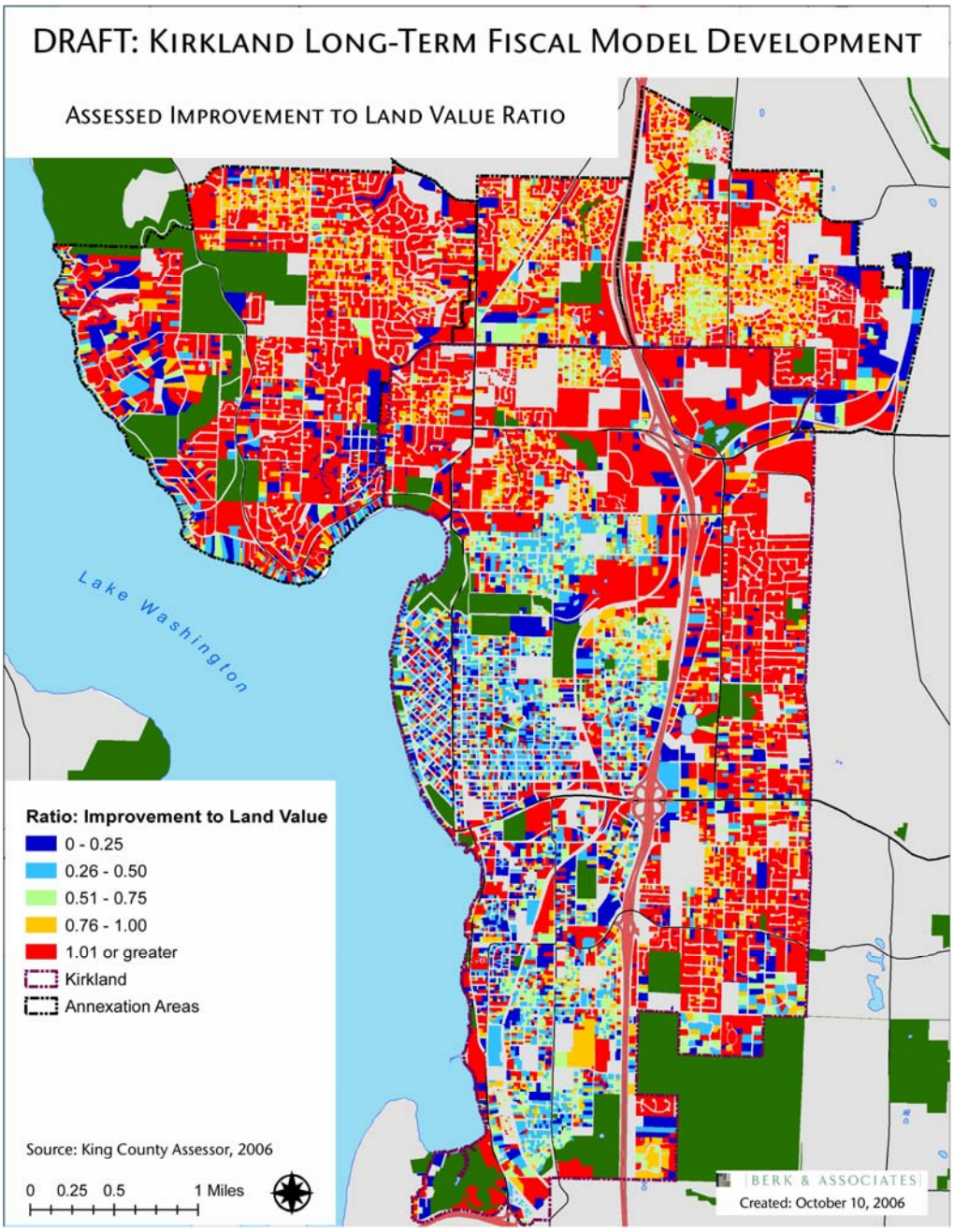
LAND VALUE

- There are clear patterns in land values on a per square foot basis, with the highest values along the water, downtown and concentrated in some of the older neighborhoods.
- There are significant differences in land values between the PAA's, areas east of I-405 and the higher value areas of the City.



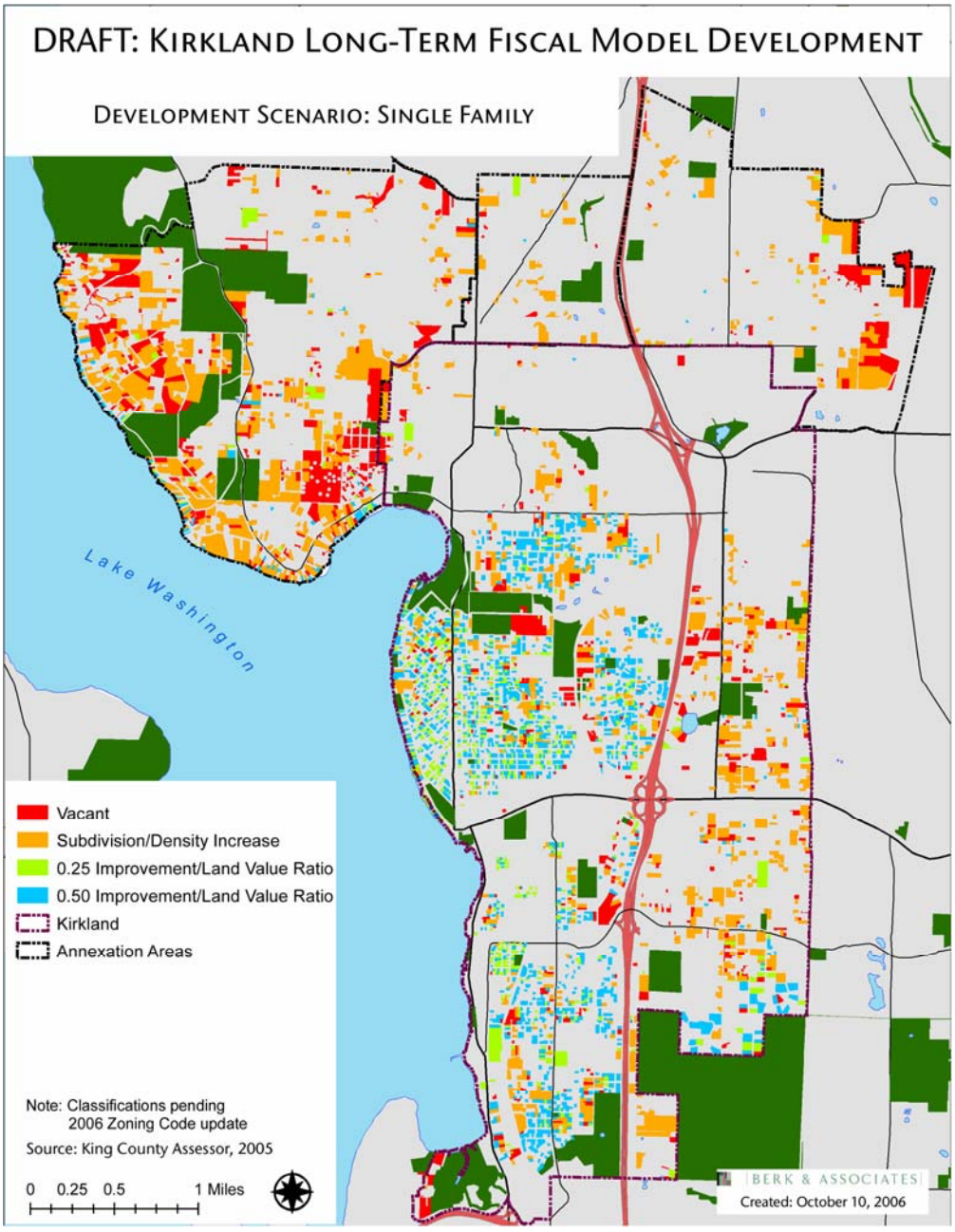
IMPROVEMENT TO LAND RATIO

- Not surprisingly many of the areas with low improvement to land ratios are located in the high land value areas and where there are older buildings. These are the areas that are likely to experience redevelopment pressures and higher rates of reinvestment in existing buildings.



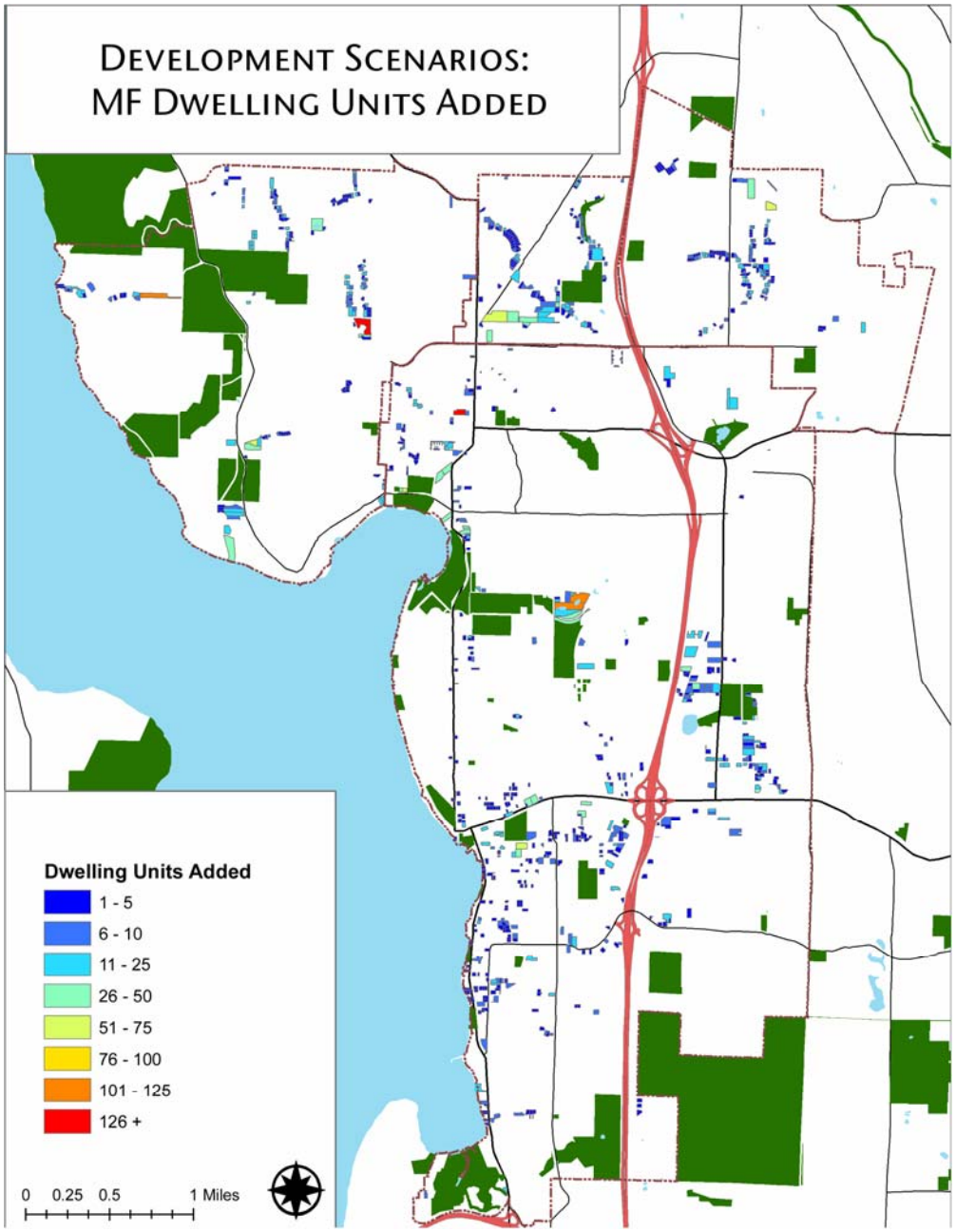
SF (VACANT, SUBDIVIDABLE, REDEVELOPABLE)

- The potential for new single-family development includes a significant number of subdividable properties in the Finn Hill and Rose Hill areas as well as redevelopment/reinvestment in the older Kirkland neighborhoods.
- A considerable number of the subdividable properties in Finn Hill are within steep slope and erosion areas, which does not necessarily reduce the development potential, but likely makes development more costly. In this case it is possible to reduce the assumed level of development in these areas.



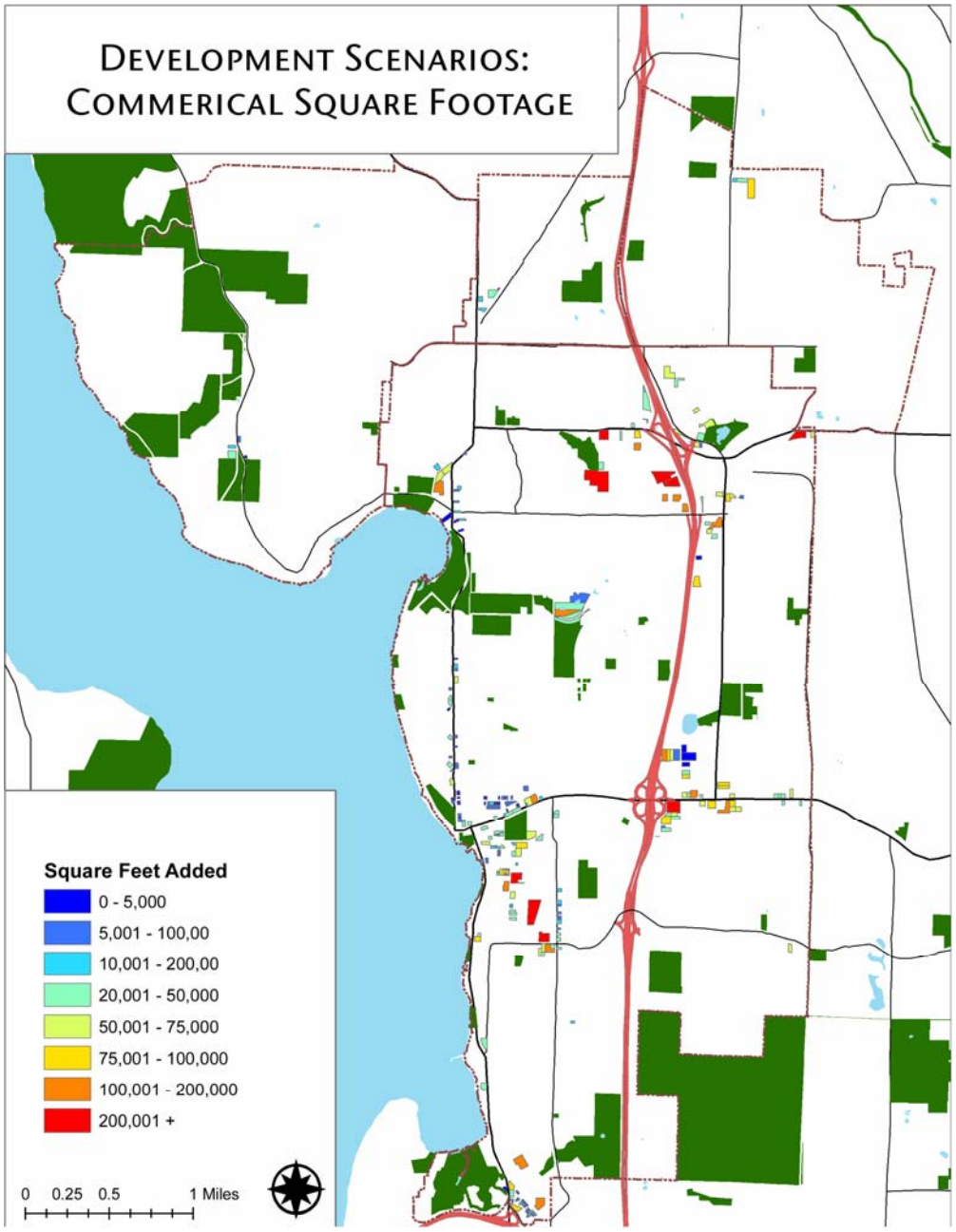
POTENTIAL FOR NEW AND REDEVELOPED MULTI-FAMILY UNITS

- Applying the same approach described above, results in the following distribution of potential new multifamily housing.
- The model allows for different assumptions about the mix of uses in the mixed use zones, such as higher residential or commercial mixes.



POTENTIAL FOR NEW AND REDEVELOPED COMMERCIAL/INDUSTRIAL SQUARE FOOTAGE

- Applying the same approach described above results in the following distribution of potential new commercial activity.
- This map assumes no rezoning, though the model does allow for testing the potential of rezoning or adding density throughout the City or PAA's.



ESTIMATING CHANGES IN DEMAND AND COST OF SERVICES

The model estimates changes in the cost of services based on relationships between direct services, such as maintenance workers or planners and underlying demographic and community changes such as increases in population, housing units, commercial activity and area.

- Costs are broken up into labor and non-labor categories.
- Non-labor costs in each department are driven by the labor costs in that department.
- Drivers for labor costs are variable in the model, and generally fall into one of four categories:
    - **Fixed.** These positions do not change over the planning horizon (for instance, there will always be one City Manager or one Police Chief).
    - **Direct.** These positions are driven directly by changes to the underlying land base of the city, such as population or employment. The relationship between demand for services and the underlying land base is largely defined based on the 2005 annexation service packages which identified how each department would be affected by growth in these key variables.
    - **Indirect (by Position).** These positions are driven by staffing levels of one or more positions in a specific department. For instance, a planning supervisor is related to the need for new associate planners, planners and senior planners.
    - **Indirect (by Department).** These positions are driven by staffing levels of one or more departments. For instance, a human resource analyst position is related to total new staffing levels in most other City departments.
- By accounting for the indirect to direct relationships, when a direct service position is added, the model ensures an increment of indirect support necessitated by the addition of the direct service.

POLICY OPTIONS TO ADDRESS COST OF SERVICES

- The policy options available to "balance the budget" include:
    - Changing assumptions about the underlying relationship between direct services and the demand drivers or between the direct staff positions and the indirect positions.
    - Changing assumptions about hiring rates. The model uses the current relationships between direct services and the demand drivers or between the direct staff positions and the indirect positions to determine when new positions are needed in response to growth. It is possible to adjust the hiring rate by either reducing it (would require more growth to trigger the next staff hire) or increasing it (would require less growth to trigger the next hire).
    - Changing assumptions about the expected escalation in key cost centers, such as salary and benefit costs per person and general inflationary costs in non-labor cost categories.

ESTIMATING TAX AND FEE REVENUES

- Tax and fee revenues are estimated based on the changes in the components of the City's tax base resulting from growth (with or without annexation). Components of growth which could influence revenue growth include population, employment, base inflation in certain components of the tax base, or land use changes,
- Each of the City's tax and fee revenue sources is separately estimated by estimating changes in the tax base and applying current tax and fee rates to generate revenue projections.
- To give the Council a full list of potential tax policy choices and the ability to model different tax policy options, the estimated tax base is included for all major potential City taxes (even those not currently imposed).

POLICY OPTIONS TO ADDRESS TAX REVENUES

- The model has the ability to assess changes in potential tax and fee revenues on properties, businesses, and utilities by varying the rate of taxes and fees and/or varying the assumptions about growth in the various components of the tax base. For example:
    - Options are available to assess different property tax scenarios including levy lid lifts and excess levies (which would require voter approval).
    - Options are available to change the tax and fee rates of existing sources (some of which would require voter approval and others which would not).
    - Options are available to add new taxes and fees on businesses and/or residents.

COMPARISON WITH 2005 STUDY RESULTS

- The exhibit below demonstrates how the current model's annexation impacts on FTEs compare to those identified through annexation service packages in the 2005 annexation study.

Annexation Impact Comparison, 2005 Study to Current Model

	Annexation FTEs		
Department	2005 Study	Current Model	Change
Nondepartmental	0.00	0.00	0.00
City Council	0.00	0.00	0.00
City Manager	1.50	1.50	0.00
Human Resources	2.00	2.00	0.00
City Attorney	1.50	1.50	0.00
Parks Community Services	6.93	6.93	0.00
Public Works	17.24	17.24	0.00
Finance Administration	5.05	5.05	0.00
Planning Community Development	9.50	9.50	0.00
Police	77.50	64.50	-13.00
Fire Building	10.00	10.00	0.00
Municipal Court	8.24	6.92	-1.32
Total	**139.46**	**125.14**	**-14.32**

- The biggest change in the base operating and maintenance impact came from the Police Department, which reduced its annexation FTE request by 15 FTEs (currently, the model only includes a reduction of 13 FTEs, as 2 are contingent on Police having its 2007-08 Budget Service Package fully funded).
- The Municipal Court, where many employees are driven directly by Police staffing levels, also sees a decrease in annexation-related FTEs.
- The net effect of these FTE changes is to reduce ongoing costs by $1.8 M, or 12%, and to reduce one-time costs by $450,000, or 7%.
- Due to the current availability of more precise data from the Department of Revenue, sales tax revenues are higher than assumed in the 2005 study.

OTHER KEY ASSUMPTIONS

- The initial baseline analysis does **not** include the need for additional firefighting personnel related to the Kingsgate station. The model does have the ability to add these contingent positions for fire protection.
- Two other key assumptions are the pre-FTE inflation rates of salaries and benefits, which have both been reduced in the 2011-2025 timeframe from levels predicted in the Base Kirkland Forecast. This reflects the fact that the model is a long-term fiscal model where the compounding effects of inflation rates can be quite large, and the shorter-term assumptions used in budgeting are not likely to be sustainable over time.

PRELIMINARY FINDINGS

- Based on the current assumptions about baseline conditions, the following are the key findings to date (see more detailed findings in **Attachment A**):
    - The City has a long-term fiscal challenge regardless of whether the City chooses to pursue annexation of the PAA's or not.
    - The base fiscal challenge facing the City will not be made worse as a result of annexation and in most cases annexation makes enhances the City's ability to address the base challenge.
    - Even without the state sales tax credit, the impact of annexation on an *operating basis* (including equipment capital but excluding facilities and infrastructure) is equal to or less than the existing City operating fiscal imbalance. This is the result of several factors:
        - Costs of PAA services are lower than the 2005 analysis because of fewer FTE's
        - Revenues are higher primarily due to higher sales tax on construction
        - Growth in incremental revenues from the PAA's is able to keep up with cost inflation due to higher development activity, especially in the outer years.
    - The incremental cost of new facilities (City Hall, police and maintenance) that are necessary to support the larger post-annexation city are a substantial challenge, as they are significantly higher than those for a no annexation scenario.
        - The almost $50 million incremental cost associated with annexation would likely require a "subsidy" from existing city to fund these improvements.
        - In cases where policies to address the base fiscal challenge result in a net positive benefit from annexation, funds would be available to offset some of the facility cost impacts.
    - The state sales tax credit is something of a "wild card" in this analysis, since the rules for which costs will be eligible have not been fully developed. If Kirkland is unable to qualify for all of the potential sales tax credit, it is unlikely the City would pursue annexation, since the PAAs simply do not have the ability to generate enough revenues to cover the total incremental costs, including the facilities to house the new staff required by annexation. If Kirkland is able to qualify for the maximum allowable credit, then annexation would appear to be fiscally viable on both an O&M basis, including the need to address related facilities.
    - Since the City cannot operate at a deficit, the Council will need to make appropriate policy adjustment to close the fiscal gap in the future ***with or without annexation***. Depending on which measures are selected, the economics of annexation will vary.
        - To assess the sensitivity of the basic PAA fiscal findings a series of alternative policy scenarios were developed using the framework shown in **Attachment B.**
        - In most cases, annexation lessens the severity of policies needed to address the baseline fiscal challenges. By increasing its size, Kirkland would effectively lengthen the

various policy levers it has to balance its budget, allowing the City to use a lighter touch with those levers. **Attachment C** provides a summary of several alternative "balanced budget" scenarios and the relative impact on the economics of annexation.

- There are likely to be more needs for infrastructure capital than there will be capital resources coming from the PAA's. This situation is comparable to the base City situation and unless there are significant immediate capital infrastructure needs in the PAAs, then the long-term funding situation is unlikely to be dramatically different than the status quo. When capital infrastructure needs are more fully assessed as part of Phase II of the annexation analysis, it will be possible to more fully assess infrastructure capital portion of the impact of annexation.
    - While the model provides estimates of the revenues from the Real Estate Excise Tax and the capital portion of the Gas Tax, they are not included in operating revenues. Nor are they used to cover any of the equipment or facility related capital needs. Instead, they are held aside as available infrastructure capital funding pending the Phase II analysis of capital infrastructure needs in the PAAs.

Facility Needs

- The City of Kirkland has facility needs regardless of the decision on annexation, though the annexation decision would dramatically increase those needs. An annexation scenario increases total facility needs by approximately $50 million:
    - **Base City Facility Needs -- $29.6 million**
        - City Hall expansion and public safety: $25 million
        - Maintenance facility expansion: $4.6 million
    - **City Needs with Annexation -- $80.7 million**
        - City Hall expansion: $28.9 million
        - New public safety and jail facilities: $44.0 million
        - Maintenance facility expansion: $7.8 million
- The 2005 annexation analysis included a $1.6 million per year charge for facility impacts resulting from annexation based on the debt service for a 30-year bond to pay for specific improvements. The cost was determined based on a "fair share" of new facilities using the number of FTE's to allocate costs. The analysis assumed a PAA facility cost allocation of $ 25.6 million, comprised of the following shares for specific improvements:
    - City Hall expansion: $6.6 million
    - Maintenance center expansion: $3.2 million
    - New public safety building: $15.8 million
- The $50 million estimate likely overstates the "true incremental cost" for two reasons:
    - The property owners in the PAA's will, upon annexation, contribute to existing voted-G.O. debt. This will reduce existing City taxpayer burden. From an equity perspective this can be

considered an offset against the incremental cost of facilities due to annexation. The present value of these taxpayer savings is approximately $2.2 million.

- Regardless of the annexation decision, the City will need to address the base City facility needs. For the purposes of analysis, one could assume that this base need would be funded through a new voted G.O. bond. If this were done, the millage rate to repay these bonds could be applied to the PAA annexation areas to develop a credit that would reflect a balanced base City situation. This credit would be worth approximately $10.5 million.

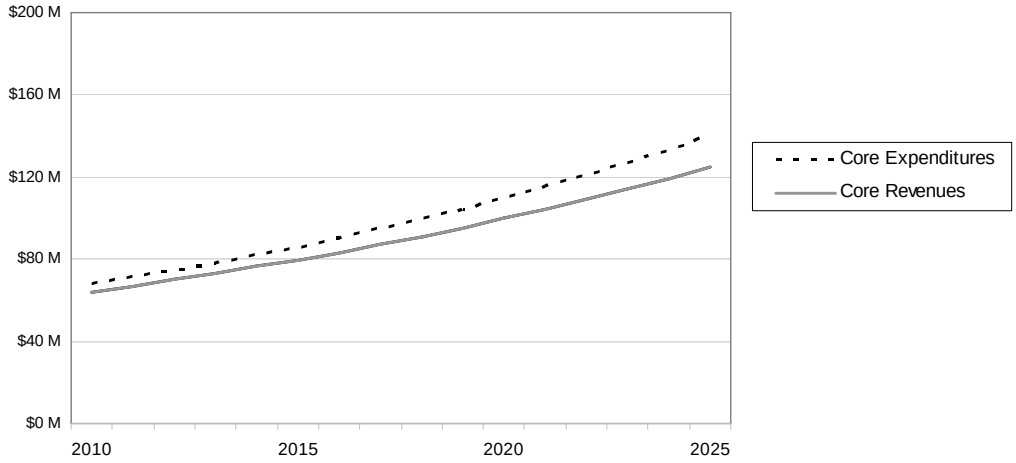
- Adjusting the incremental estimate to account for these credits results in a PAA facility cost impact of $38 million. As a result, the annual facility cost impacts could range from a low of $1.6 million per year for a "fair share" approach to a high of $2.7 million per year for an incremental approach.

- There are a number of issues that will influence how facility impacts might be viewed, in particular the eligibility of these costs for sales tax credit and how one interprets potential changes in annexation economics resulting from policy changes to address base fiscal challenges.

ATTACHMENT A:

BASELINE SCENARIOS (UPDATED FEBRUARY 2007)

Scenario: Baseline No Annexation

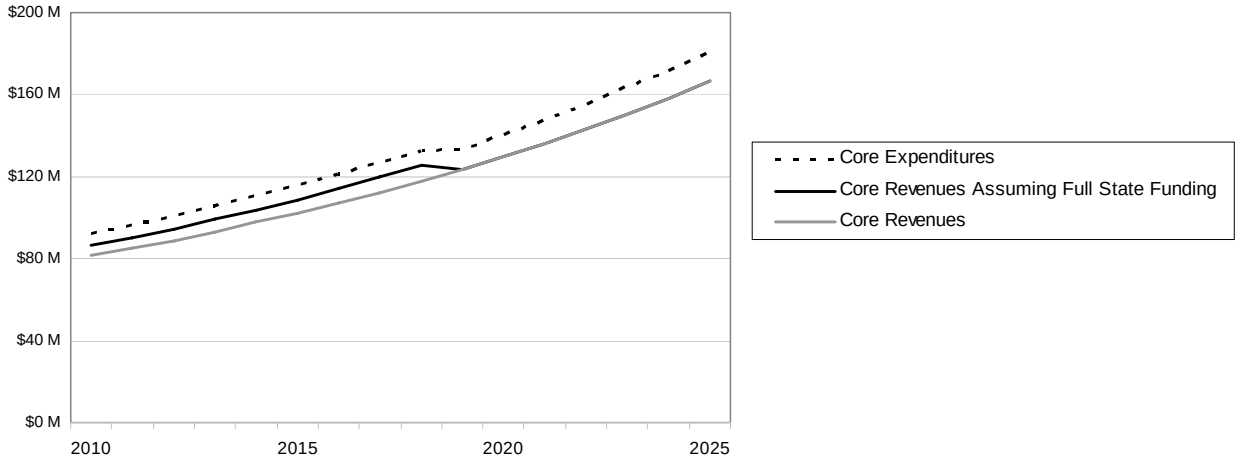


Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,804	83,604	107,673	138,105
Facility Debt Service (000's)	2,295	2,295	2,295	2,295
Subtotal Expenditures	**68,099**	**85,899**	**109,968**	**140,400**
Core Resources (000's)	64,000	79,685	99,650	124,937
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,000**	**79,685**	**99,650**	**124,937**
Net Resources (000's)	**(4,099)**	**(6,214)**	**(10,318)**	**(15,462)**
Deficit as % of Expenditures	**-6%**	**-7%**	**-10%**	**-11%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	0	0	0	0
Facility Debt Service (000's)	0	0	0	0
Subtotal Expenditures	**0**	**0**	**0**	**0**
Core Resources (000's)	0	0	0	0
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**0**	**0**	**0**	**0**
Net Resources (000's)	**0**	**0**	**0**	**0**
Deficit as % of Expenditures	**N/A**	**N/A**	**N/A**	**N/A**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	65,804	83,604	107,673	138,105
Facility Debt Service (000's)	2,295	2,295	2,295	2,295
Subtotal Expenditures	**68,099**	**85,899**	**109,968**	**140,400**
Core Resources (000's)	64,000	79,685	99,650	124,937
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,000**	**79,685**	**99,650**	**124,937**
Net Resources (000's)	**(4,099)**	**(6,214)**	**(10,318)**	**(15,462)**
Deficit as % of Core Expenditures	**-6%**	**-7%**	**-10%**	**-11%**

Scenario: Baseline With Annexation



Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,843	83,819	107,752	138,083
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**68,153**	**86,129**	**110,042**	**140,330**
Core Resources (000's)	64,326	80,067	100,110	125,510
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,326**	**80,067**	**100,110**	**125,510**
Net Resources (000's)	**(3,827)**	**(6,062)**	**(9,932)**	**(14,820)**
Deficit as % of Expenditures	**-6%**	**-7%**	**-9%**	**-11%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,079	22,751	29,565	39,117
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**23,953**	**29,624**	**30,587**	**40,181**
Core Resources (000's)	16,507	21,557	28,618	39,902
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**21,433**	**28,123**	**28,618**	**39,902**
Net Resources (000's)	**(2,520)**	**(1,502)**	**(1,969)**	**(279)**
Deficit as % of Expenditures	**-15%**	**-7%**	**-7%**	**-1%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,922	106,569	137,317	177,200
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**92,106**	**115,753**	**140,628**	**180,511**
Core Resources (000's)	80,833	101,624	128,727	165,412
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**85,759**	**108,190**	**128,727**	**165,412**
Net Resources (000's)	**(6,347)**	**(7,564)**	**(11,901)**	**(15,099)**
Deficit as % of Core Expenditures	**-8%**	**-7%**	**-9%**	**-9%**

ATTACHMENT B:

FRAMEWORK FOR EVALUATING ALTERNATIVE POLICY SCENARIOS

ANNEXATION FISCAL POLICY

Tools and Scenarios

Tools

1. Development-related revenue
   - new construction property tax
   - sales tax
2. Tax policy revenue
   - property tax
   - utility tax
   - business tax
3. Expenditure management
   - level of service – staffing levels
   - efficiency/productivity
   - compensation

Scenario Options

Varying emphasis on specific tools

High (H)

Medium (M)

Low (L)

Options (as examples)

Tools	Development	Tax	Expenditure
Option 1	M	L	H
2	L	H	M
3	M	M	M
4	H	L	L

Fill in numbers for the above options – show math and results

ATTACHMENT C:

SENSITIVITY ANALYSIS OF ALTERNATIVE FISCAL POLICY OPTIONS ON THE ECONOMICS OF ANNEXATION (UPDATED FEBRUARY 2007)

	Tools			Long-Term Fiscal Outlook		
	Tax Policies	Expenditure Management Policies	Development	Fiscal Analysis Findings		Net Impact of Annexation
Baseline No Annexation	No change in tax policy 1% property tax limit	Hiring rate reflects current policies	Baseline	**O&M Impacts** Deficits in all years Deficit grows to $15.5M by 2025 Def. as % of exp.: 1% to 11% Cost growth: 5.1%/yr Revenue growth: 4.5%/yr	**Facilities** $30 M unfunded need Annual D/S: $2.3 M	**Surplus/Deficit in 2025** Current Kirkland: ($15.5M) PAA: 0.0M Total City: (15.5M)
Annexation Scenarios						
Baseline With Annexation	Same as above	Same as above	City: Baseline PAA: Baseline	**O&M Impacts** Citywide deficit marginally reduced PAA deficit starts at 15% and ends at 1% Cost growth:6.4%/yr Revenue growth: 6.0%/yr	**Facilities** $80 M need citywide $38 M impact from annexation 30-year bond -- $3.3M/yr (all city) 10-year bond -- $5.9M/yr (PAA impact)	**Surplus/Deficit in 2025** Current Kirkland: ($14.8M) PAA: (0.3M) Total City: (15.1M)
Balanced Scenarios (closes fiscal gap to within 1% of Expenditures in 2020)						
Property-Tax Focused	**High** Same as baseline plus the following levy limits: 2010-2015: 4.0% 2016-2025: 3.5%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	**Medium** City: Baseline PAA: Baseline	Balancing with primarily property tax results in net gains from the annexation areas which help offset base City structural deficit issues. Without annexation, tax rates would need to be higher to achieve the same ends.		Current Kirkland: ($4.1M) PAA: 4.6M Total City: .5M
Business-Tax Focused	**High** Same as baseline plus a new business tax on gross receipts at 0.0975%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	**Medium** City: Baseline PAA: Baseline	This scenario is similar to the property tax based scenario except the net contribution from annexation is smaller, since the tax is based on busineses only.		Current Kirkland: ($5.7M) PAA: 2.9M Total City: (2.8M)
No Growth-Related Hiring, Balance With Property Tax	**Medium** Same as baseline plus the following levy limits: 2010-2015: 3.0% 2016-2025: 2.5%	**High** Reduce rate of hiring: hired 47 fewer FTEs (185 to 138)	**Medium** City: Baseline PAA: Baseline	The impact of much lower hiring reduces the need for new taxes, though at a likely cost in terms of level-of-service. The impact of annexation is even more positive as the rate of growth in the annexation areas is somewhat higher than current Kirkland.		Current Kirkland: ($4.4M) PAA: 6.4M Total City: 1.9M
Low Development PAAs, Property-Tax Focused	**High** Same as baseline plus the following levy limits: 2010-2015: 5.0% 2016-2025: 4.5%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (179 to 174)	**Low** City: Baseline PAA: Low	The impact of lower PAA development is higher tax rates and a lower FTE demand overall, though the PAA fiscal impact remains positive and the taxes lower than a no annexation scenario.		Current Kirkland: ($1.8M) PAA: 2.2M Total City: .4M
High Development Current City, Property-Tax Focused	**Low** Same as baseline plus the following levy limits: 2010-2015: 3.0%	**Medium** Reduce rate of hiring: hired 7 fewer FTEs (192 to 185)	**High** City: High PAA: Baseline	The impact of high development in current Kirkland is a much lower tax need. The impact of annexation remains positive, but to a much lower degree, since most of the funding gap is solved by development in current Kirkland.		Current Kirkland: ($2.9M) PAA: 1.9M Total City: 1.0M

CITY OF KIRKLAND
Department of Finance & Administration
123 Fifth Avenue, Kirkland, WA 98033 425.587.3100
www.ci.kirkland.wa.us

MEMORANDUM

To: David Ramsay, City Manager

From: Tracey Dunlap, Director of Finance and Administration
Marilynne Beard, Assistant City Manager

Date: January 5, 2007

Subject: Annexation Fiscal Analysis – Study Session #2

RECOMMENDATION:

Council continue its discussion of the annexation fiscal analysis and additional public outreach to be conducted as part of Phase I.

BACKGROUND DISCUSSION:

At the December 12, 2006 Study Session, the City Council received the preliminary draft findings of the Annexation Long-Term Fiscal Analysis. At that meeting, a process for evaluating the results was discussed and additional information was requested. The supplemental information will be presented at the January 9, 2007 Special Study Session, including:

- Additional details regarding the baseline assumptions related to development, revenue projections, and expenditures, such as:
  - Projected development by type (single family, multifamily, commercial),
  - Assumed revenues, including historical sales tax trends,
  - Projected expenditures, including the major drivers of staffing additions and further detail on updated assumptions from the 2005 analysis, particularly related to Public Safety;
- Further details on the facilities financing assumptions and the state sales tax credit;
- Descriptions of the development, revenue, and expenditure assumptions in the "High, Medium, and Low" emphasis scenarios;
- An overview of the variables that most influence the results; and
- Updated scenarios and related materials.

The presentation slides and related supplemental information are attached to this memorandum. If you have questions while reviewing the materials that you would like to discuss before the January 9 meeting, please call Tracey at x3101. This information, along with the more detailed description of the model and policy issues that was contained in the December 12 Council packet, is intended to provide the City Council with sufficient financial information to enable a decision on whether to proceed to Phase 2 of the

annexation evaluation. Staff has been working with the City's communications consultants to develop options for an extended outreach process, which are outlined in the discussion that follows.

Public Outreach Plan

At the November 21st Council meeting, Sarah Brandt from EnviroIssues provided a recap of the phase one public outreach activities and results. At that time, Council expressed an interest in extending phase one to include additional outreach focusing on the results of the annexation fiscal analysis. At the December 12th meeting, staff suggested a process that continued Council discussion of the financial analysis in early January (special study session on January 9th), continued community outreach into late January/early February with a public forum in February and a concluded with phase one "go/no go" decision in early March. Since that time, the City's consultants have worked with staff and the annexation subcommittee to better define the format for the extended public outreach effort. EnviroIssues identified two format options for consideration including focus groups and a public forum. The format is described below:

> ***Convene a public meeting or forum (beginning with an open house and including a presentation) to discuss financial information. Provide an opportunity for input in one of two ways:***
>
> 1. ***Hold meeting at City Hall's Peter Kirk Room, then invite attendees into Council Chambers to participate in a "town meeting" discussion (i.e., Council listens while facilitator passes a microphone through the crowd for comments, rather than a hearing format). Council would not necessarily respond to each comment, but each member would have the opportunity to make a statement at the end of the discussion.***
>
> 2. ***Split attendees into small facilitated groups, with Council members in each group, and discuss reactions to the financial information and other factors influencing public opinions. Upon regrouping and debriefing, Council members could make statements to close the meeting.***

The options were reviewed with the annexation subcommittee at their January 4th meeting and the recommendation is to implement option one using a town hall meeting format to obtain public comment. Prior to the public forum, the findings of the financial analysis will be made available through our annexation listserv, on the City's web page and other means as available.

The public forum will have four general components that take place over a three hour period:

1. **Open House Workshop –** The public will be invited to learn more about the financial analysis, to ask questions of the staff and consultant and to see a demonstration of the model. The listening log results will be posted around the room and a board will be displayed showing the "top ten" questions asked during the public outreach process and the answers (when available). The open house portion will last one hour.

2. **Presentation –** Staff will make a presentation summarizing the findings of the financial analysis including responses to the most frequently asked financial questions. Following the presentation, the audience will have an opportunity to ask questions. The question period will be facilitated by the consultant using a "town hall" format whereby they consultant moves through the audience with a microphone to obtain questions with staff answering questions as appropriate. The presentation and question period will last about 30 to 45 minutes.

3. **Public Comments –** After the presentation and related questions, the consultant will solicit comment from the audience using the same town hall format used for the question phase. The purpose of the comments session is to obtain input regarding any further concerns the Kirkland community may have that they believe should be addressed by the City Council. The comment period will last up to one hour.

4. **Closing Comments –** The last 15 minutes will be reserved for Council Member comments.

If possible, the forum will be held at the Peter Kirk Community Center since it has the capacity to accommodate an open house format with information boards as well as a town hall audience format without having to move from one room to another.

If Council agrees with this general approach, staff will begin to schedule and plan for the expanded outreach program. Since this is an expansion of the work first envisioned in our consultant's phase one scope of work, we are requesting Council approval of additional funding of up to $9,420 for the consultants to develop new outreach materials, prepare for the public forum and facilitate the large and small group discussions.

City of Kirkland

Annexation Fiscal Analysis

Council Study Session #2

January 9, 2007

Presentation Overview

- Recap of key points from December 12
- Additional Detail – Baseline Assumptions
  - Kirkland Base Results
  - Kirkland Base with Annexation
- Description of Scenario Assumptions
  - Selected Scenario Results
- Next Steps and Community Outreach

Objectives

- Provide responses to specific questions and requests from December 12, 2006 Study Session
- Provide a basis for discussion of policy tools and scenarios
- Provide Council with sufficient financial information to enable a decision on whether to proceed to Phase 2 of the annexation evaluation

The Big Picture

- Kirkland has a structural imbalance between revenues and expenditures
- There is a resulting long-term gap in funding
- The Council will have to close that gap with or without annexation
- Annexation could help close the gap in the long term because there are more people contributing to whatever the solution is

Past Strategies for Closing the Gap*

Strategy	< 1999	1999	2000	2001	2002	2003	2004	2005-06
New revenue source:								
Surface water management fee	X							X
Revenue generating regulatory license fee						X		
Surface water utility tax					X			
Cost of service interfund charge	X							
Increased tax rate or fee:								
Increased property tax rate	X		X			X	X	X
Increased utility tax rate						X		X
Increased parking fines			X		X			
Increased development fees		X	X		X			
Changes to sales tax:								
Reduced CIP allocation			X					
Reduced sales tax lag to 1 year								X
Used one-time revenue source:								
Sales tax audit proceeds							X	
Interest income								X
Planned use of Rainy Day reserve						X	X	X
Expenditure reductions					X	X	X	
Other strategies:								
Used new construction growth	X	X						
Reduced budgeted benefit rate to citywide average					X			X
Reduction in state retirement rates					X			

* Additional information is included in the supplemental packet.

Baseline Assumptions and Related Information

Baseline Assumptions

- ***"Baseline" is defined as current conditions with no change in policy, for example:***
  - Baseline represents the "medium" development assumptions, which are similar to the pace of development generally planned for by the City
    - No explicit decisions are made that encourage or discourage the pace of development
  - The low and high development scenarios are intended to test how sensitive the projections are to the pace of development

Development Scenario Characteristics – Average*

Development Scenarios and Outputs (AVERAGE PER YEAR)

	Current City			PAAs			Total City		
	Low	Baseline	High	Low	Baseline	High	Low	Baseline	High
Residential									
SF DU Developed/Year	117	171	255	64	103	139	181	273	394
Net SF DU Added/Year	77	97	97	53	84	111	130	181	208
MF DU Developed/Year	159	206	232	77	125	161	236	331	393
Net MF DU Added/Year	135	171	174	68	110	143	203	281	317
Commercial									
Net Sq Ft Added (Retail)/Year	55,661	54,299	124,941	16,558	27,533	43,479	72,219	81,831	168,419
Net Sq Ft Added (Non-retail)/Year	14,792	100,840	143,454	22,927	36,867	57,212	37,719	137,707	200,667
Net Sq Ft Added (Total)/Year	70,453	155,139	268,395	39,485	64,399	100,691	109,938	219,538	369,086

SF DU – Single Family Dwelling Unit

MF DU – Multi-Family Dwelling Unit

* Additional information is included in the supplemental packet.

Cost of Service Assumptions

- Model estimates changes in the cost of services based on demand drivers for direct services, such as demographics and community changes
- The policy options available to change the cost of service include changing assumptions about:
  - Expected escalation of salary and benefit costs per FTE
    - Salaries escalate at 6% through 2010 and 5% thereafter
    - Benefits escalate at 10% through 2010 and 6% thereafter
  - Demand drivers that generate the need for staff to provide services (rate of hiring)

Description of Labor Categories

- **Direct.** Positions are driven directly by changes to the underlying land base of the city, such as population or employment
- **Fixed.** Positions do not change over the planning horizon
- **Indirect.** Positions are driven by staffing levels of one or more positions in a specific department or several departments

Examples of Direct Demand Drivers

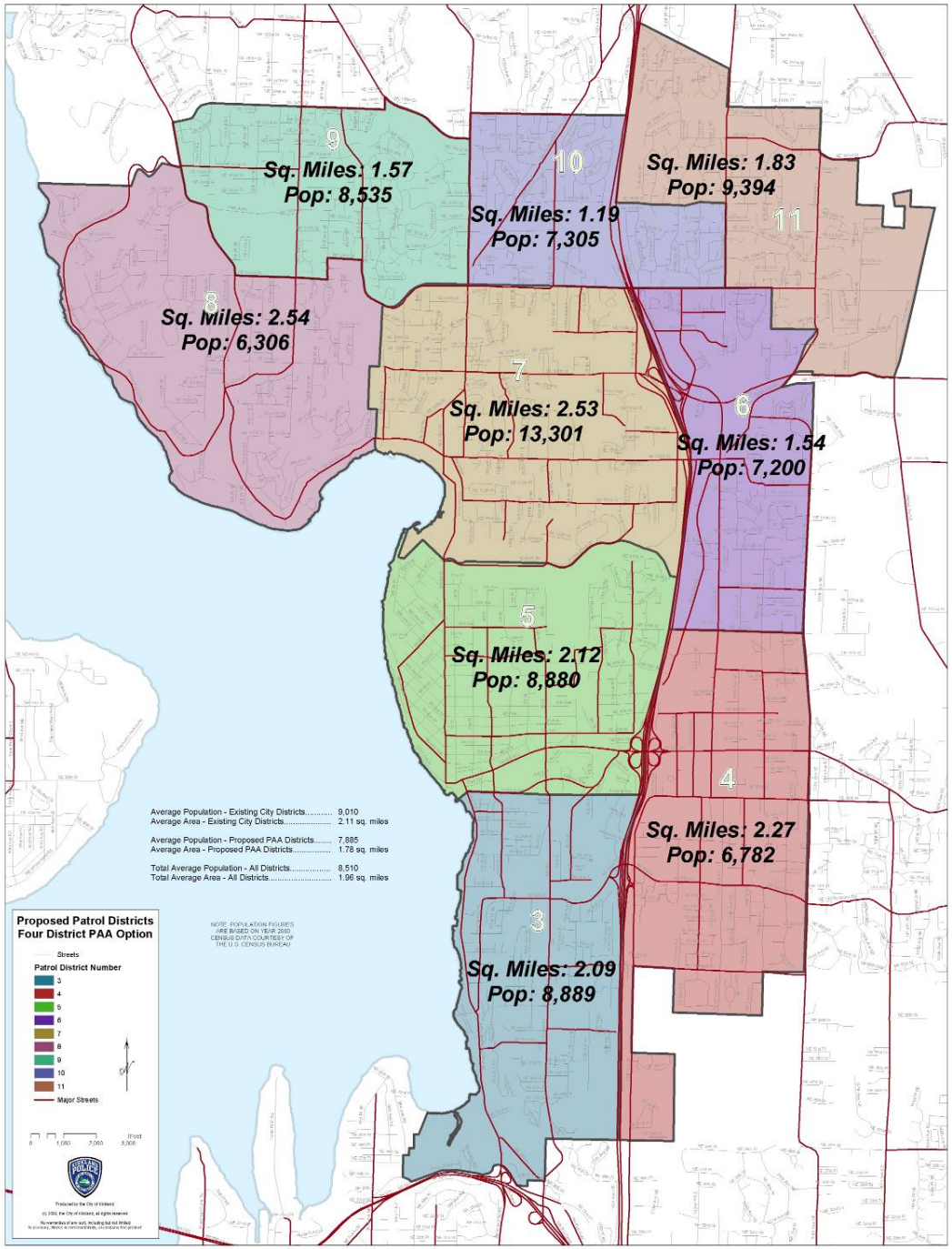
Position	FTE's (2006)	Driver
PARKS & COMMUNITY SERVICES		
Recreation Coordinator	1.00	Total Population (100%)
Groundsperson	10.50	Park Area (Acres) (100%)
PUBLIC WORKS		
Development Engineer	1.00	Total Population (100%)
Senior Maint. Person	3.50	Land Area (SqM) (100%)
Utilityperson	4.00	SF Dwelling Units (Total) Base (100%)
PLANNING & COMMUNITY DEVELOPMENT		
Senior Planner/Planner	8.67	Total Pop. (30%), Total Jobs (End of Year) (30%), Land Area (SqM) (30%)
Associate Planner	2.00	Total Population (100%)
Code Enforcement Officer	2.00	Total Dwelling Units (100%)

Comparison of FTEs to 2005 Results

Department	Annexation FTEs 2005 Study	Annexation FTEs Current Model	Change
Nondepartmental	0.00	0.00	0.00
City Council	0.00	0.00	0.00
City Manager	1.50	1.50	0.00
Human Resources	2.00	2.00	0.00
City Attorney	1.50	1.50	0.00
Parks Community Services	6.93	6.93	0.00
Public Works	17.24	17.24	0.00
Finance Administration	5.05	5.05	0.00
Planning Community Development	9.50	9.50	0.00
Police	77.50	64.50	-13.00
Fire Building	10.00	10.00	0.00
Municipal Court	8.24	6.92	-1.32
Total	**139.46**	**125.14**	**-14.32**

Key Changes to Public Safety Figures

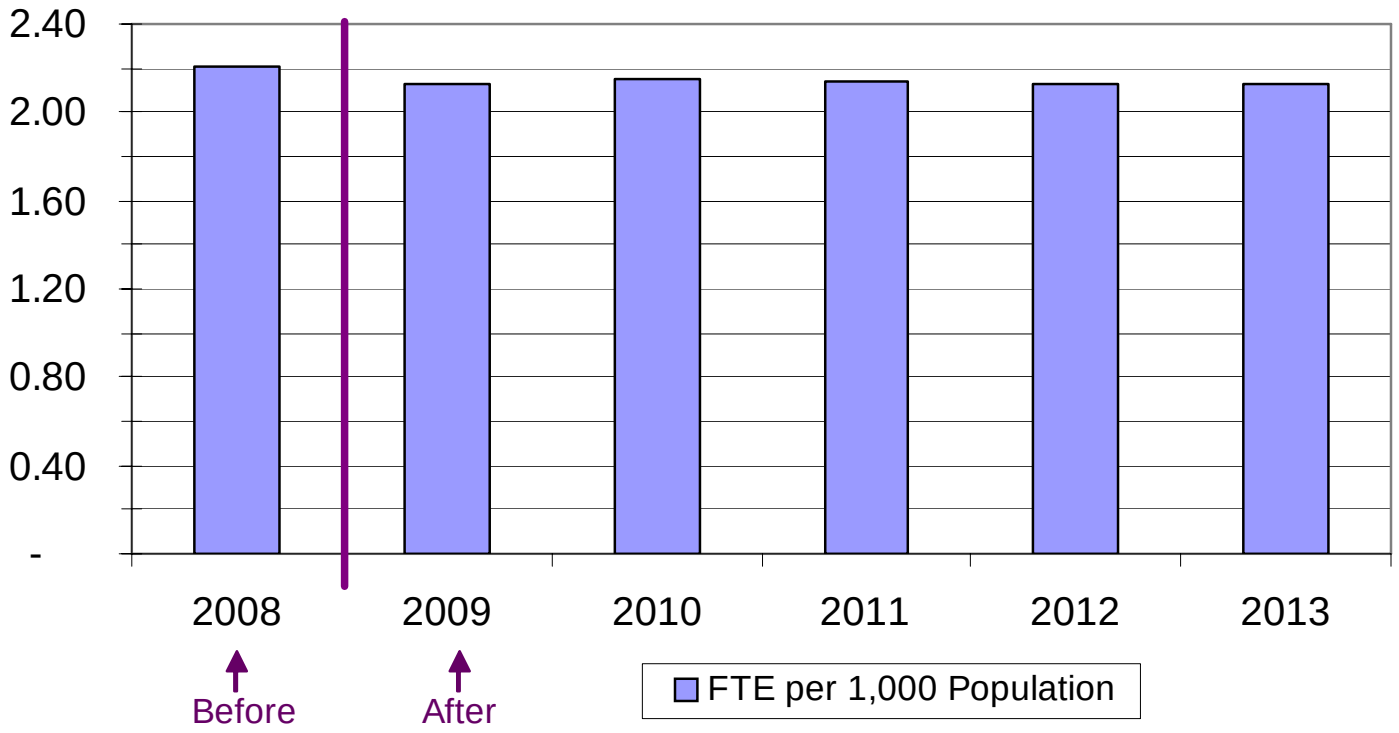
- Refinement of support position projections
- Looking at service for City and PAA as a whole
- Four patrol districts versus five, recognizing economies of modifying existing patrol district boundaries


9
Sq. Miles: 1.57
Pop: 8,535
10
Sq. Miles: 1.19
Pop: 7,305
Sq. Miles: 1.83
Pop: 9,394
11
8
Sq. Miles: 2.54
Pop: 6,306
7
Sq. Miles: 2.53
Pop: 13,301
6
Sq. Miles: 1.54
Pop: 7,200
5
Sq. Miles: 2.12
Pop: 8,880
4
Sq. Miles: 2.27
Pop: 6,782
3
Sq. Miles: 2.09
Pop: 8,889
Average Population - Existing City Districts..... 9,010
Average Area - Existing City Districts..... 2.11 sq. miles
Average Population - Proposed PAA Districts..... 7,885
Average Area - Proposed PAA Districts..... 1.78 sq. miles
Total Average Population - All Districts..... 8,510
Total Average Area - All Districts..... 1.96 sq. miles
NOTE: POPULATION FIGURES ARE BASED ON YEAR 2000 CENSUS DATA COURTESY OF THE U.S. CENSUS BUREAU
Proposed Patrol Districts
Four District PAA Option
Streets
Patrol District Number
3
4
5
6
7
8
9
10
11
Major Streets
N
0
1,000
2,000
Feet
3,000

Key Changes to Public Safety Figures

SWORN	Original Calculation	Revised Calculation	Reduction
Administration	3.0	3.0	0
Detectives	5.0	5.0	0
Narcotics Officer	1.0	1.0	0
Patrol	36.5	30	6.5
FVU Detective	1.0	0	1.0
NRO	1.0	0	1.0
K-9	1.0	1.0	0
Traffic	4.0	4.0	0
SWORN TOTALS	52.5	44.0	8.5
NON-SWORN	Original Calculation	Revised Calculation	Reduction
Records	4.0	4.0	0
Admin Support	2.0	2.0	0
Clerk Typist	1.0	0	1.0
Evidence Officer	0.5	0.5	0
Corrections	5.0	3.0	2.0
Communications	12.0	9.0	3.0
Analyst	0.5	0	0.5
NON-SWORN TOTALS	25.0	18.5	6.5

Total Police FTEs per 1,000 Population



	2008	2009	2010	2011	2012	2013
FTE per 1,000	2.21	2.13	2.15	2.14	2.13	2.12
FTEs	103.50	170.00	172.50	173.00	173.00	173.50

Treatment of Facilities Costs

- City has facilities needs, regardless of annexation

Base City Facility Needs	$29.6 million
City Hall expansion and public safety	$25.0 million
Maintenance facility expansion	$4.6 million

City Needs with Annexation	$80.7 million
City Hall expansion	$28.9 million
New public safety and jail facilities	$44.0 million
Maintenance facility expansion	$7.8 million

Treatment of Facilities Costs – PAA Share

- Incremental facilities cost is about $50 million
- PAA share should recognize that the PAA residents would also contribute toward facilities financed by existing City residents (for example, 40% of the improvements without annexation)
- To recognize the contribution, a credit of about $12 million dollars is applied to the PAA share
- The facilities costs attributed to the PAA totals $38 million

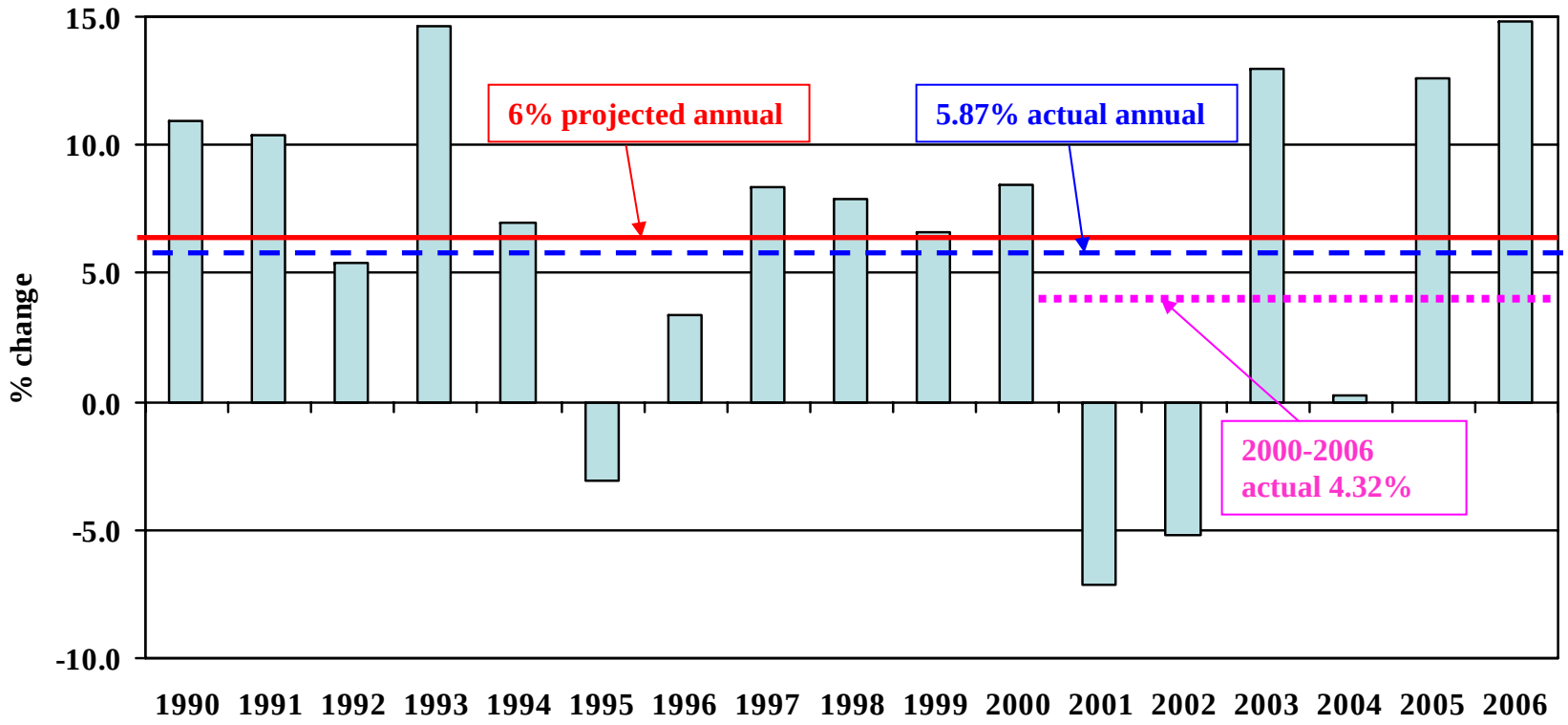
Treatment of Facilities Costs – PAA Share

- The state sales tax credit only applies for a 10 year period
- Generally, facilities would be financed over a 20-30 year period
- To match cash flow, the PAA cost share is assumed to be financed over 10 years
- In reality, this would be accomplished by one of a variety of methods such as:
  - Sinking fund payments
  - Accelerated depreciation
  - Custom debt amortization

Baseline Revenue Assumptions

- Tax and fee revenue estimates based on changes in components of the City's tax base resulting from growth (with or without annexation)
- Baseline assumptions:
  - Property tax increases by 1% optional levy each year plus new construction
  - Current business license surcharge remains in effect
  - Utility taxes remain at current rates
  - Sales tax revenues are expected to grow based on growth in retail square footage (annual increases ranging from 5.5% to 6.5%)

Sales Tax 1990-2006 Percentage Change



Totem Lake Assumptions

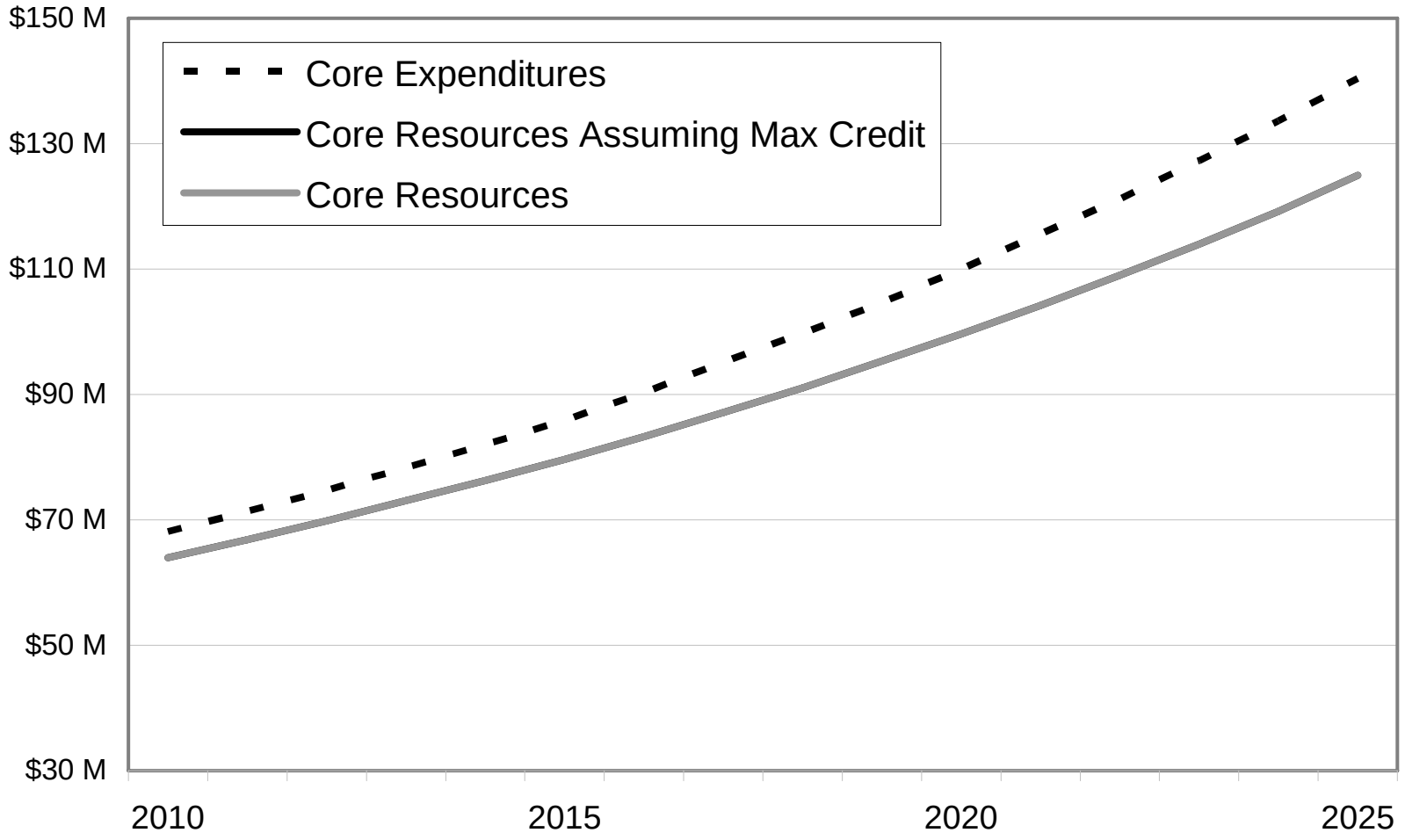
- Redevelopment 50% complete in 2008, 100% in 2009
- 216 MF Dwelling Units Added
- 620,049 sq ft Retail Added
- 144,000 sq ft Office Added
- $213,292 (2005$) Admissions Tax Bump
- $13M debt financed at 5% for 20 years

State Sales Tax Credit Issues

- Without State Sales Tax Credit, significant fiscal impact of annexation to existing City taxpayers
- Assuming maximum Sales Tax Credit revenue, overall fiscal impact is neutral to positive in the long term:
  - Fiscal impact largely offset in the 10-year period of the credit.
  - Larger tax base and potential for greater economies of scale provides greater policy leverage to address future fiscal challenges.
- Working on specific guidance regarding credit application, including use toward facilities costs

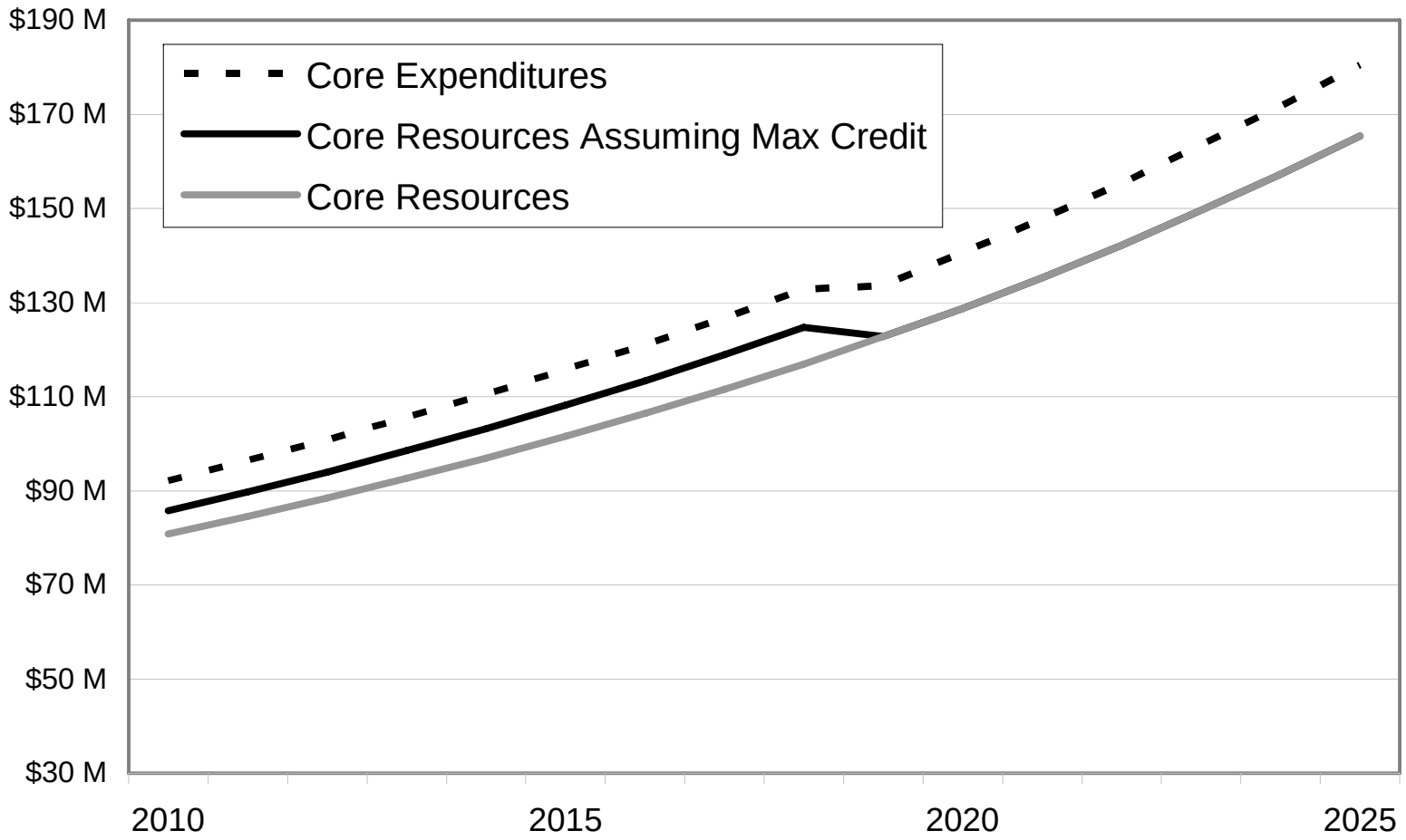
Scenario: Baseline No Annexation

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	Baseline



Scenario: Baseline With Annexation

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	City: Baseline PAA: Baseline



Scenario Assumptions and Preliminary Results

Fiscal Balancing Tools

1. Development-related revenue
   - new construction property tax
   - sales tax
2. Tax policy revenue
   - property tax
   - utility tax
   - business tax
3. Expenditure management
   - level of service – staffing levels
   - efficiency/productivity
   - compensation

Scenario Definitions

- Baseline is defined as current conditions with no change in policy
- For development only, baseline is the medium case
- For revenues and costs of service, Low, Medium, and High are all changes from the baseline assumptions
- The terms “Low, Medium, and High” refer to the *level of emphasis placed in each tool*, not necessarily the relative sizing of each option

Scenario Assumptions - Development

- Scenarios test sensitivity to the pace of development
  - Low: Rate of development 70% of baseline
  - Medium (Baseline): Rate of development consistent with pace generally planned for
  - High: Rate of development 30% higher than baseline

Development Scenario Characteristics – Total*

Development Scenarios and Outputs (TOTAL)

	Current City			PAAs			Total City		
	Low	Baseline	High	Low	Baseline	High	Low	Baseline	High
Residential									
SF DU Developed	2,338	3,413	5,106	1,282	2,055	2,775	3,620	5,468	7,881
Net SF DU Added	1,548	1,935	1,935	1,051	1,682	2,223	2,599	3,617	4,158
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Net MF DU Added	2,707	3,410	3,479	1,357	2,204	2,852	4,064	5,614	6,331
Commercial									
Net Sq Ft Added (Retail)	1,113,218	1,706,019	2,498,816	331,161	550,654	869,571	1,444,379	1,636,624	3,368,387
Net Sq Ft Added (Non-retail)	295,835	1,396,753	2,869,090	458,540	737,334	1,144,243	754,376	2,754,136	4,013,333
Net Sq Ft Added (Total)	1,409,053	3,102,772	5,367,906	789,702	1,287,988	2,013,814	2,198,755	4,390,760	7,381,720
% AV from New Construction	1.26%	1.70%	2.22%	1.44%	2.16%	2.74%	1.31%	1.84%	2.38%

* Additional information is included in the supplemental packet.

Scenario Assumptions - Revenues

- Model assesses changes in potential tax and fee revenues on properties, businesses, and utilities.

Low	
Property Tax	3.0% per year for first 6 years (voter approval)
Business Tax/Utility Tax	Remains as is
Medium	
Property Tax	2.5-3.0% per year (voter approval)
Business Tax/Utility Tax	Remains as is
High	
Property Tax[1]	3.5-5.0% per year (voter approval) OR
Business Tax	0.0975% of gross receipts OR
Utility Taxes[2]	9.0% on utilities (requires vote for private utilities)
[2]Scenario not shown in presentation, but utility tax included as part of blended scenario.	

[1] Property tax lid lift assumes use of remaining banked capacity without spending it on increased service levels

Scenario Assumptions – Cost of Service

- Assumes that new hiring rates related to growth are reduced from calculated levels
  - Low: No change - hiring based on projected needs based on service drivers (varies depending on development scenario: low 179/high 192 FTEs)
  - Medium: Hiring 5 fewer FTEs than projected
  - High: Hiring 47 fewer FTEs than projected (no new hires for growth)

Preliminary Matrix of Options*

	Tools			Long-Term Fiscal Outlook		
	Tax Policies	Expenditure Management Policies	Development	Fiscal Analysis Findings		Net Impact of Annexation
Baseline No Annexation	No change in tax policy 1% property tax limit	Hiring rate reflects current policies	Baseline	**O&M Impacts** Deficits in all years Deficit grows to $15.5M by 2025 Def. as % of exp.: 1% to 11% Cost growth: 5.1%/yr Revenue growth: 4.5%/yr	**Facilities** $30 M unfunded need Annual D/S: $2.3 M	**Surplus/Deficit in 2025** Current Kirkland: ($15.5M) PAA: 0.0M Total City: (15.5M)
Annexation Scenarios						
Baseline With Annexation	Same as above	Same as above	City: Baseline PAA: Baseline	**O&M Impacts** Citywide deficit marginally reduced PAA deficit starts at 15% and ends at 1% Cost growth:6.4%/yr Revenue growth: 6.0%/yr	**Facilities** $80 M need citywide $38 M impact from annexation 30-year bond -- $3.3M/yr (all city) 10-year bond -- $5.9M/yr (PAA impact)	**Surplus/Deficit in 2025** Current Kirkland: ($14.8M) PAA: (0.3M) Total City: (15.1M)
Balanced Scenarios (closes fiscal gap to within 1% of Expenditures in 2020)						
Property-Tax Focused	**High** Same as baseline plus the following levy limits: 2010-2015: 4.0% 2016-2025: 3.5%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	**Medium** City: Baseline PAA: Baseline	Balancing with primarily property tax results in net gains from the annexation areas which help offset base City structural deficit issues. Without annexation, tax rates would need to be higher to achieve the same ends.		Current Kirkland: ($4.1M) PAA: 4.6M Total City: .5M
Business-Tax Focused	**High** Same as baseline plus a new business tax on gross receipts at 0.0975%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	**Medium** City: Baseline PAA: Baseline	This scenario is similar to the property tax based scenario except the net contribution from annexation is smaller, since the tax is based on busineses only.		Current Kirkland: ($5.7M) PAA: 2.9M Total City: (2.8M)
No Growth-Related Hiring, Balance With Property Tax	**Medium** Same as baseline plus the following levy limits: 2010-2015: 3.0% 2016-2025: 2.5%	**High** Reduce rate of hiring: hired 47 fewer FTEs (185 to 138)	**Medium** City: Baseline PAA: Baseline	The impact of much lower hiring reduces the need for new taxes, though at a likely cost in terms of level-of-service. The impact of annexation is even more positive as the rate of growth in the annexation areas is somewhat higher than current Kirkland.		Current Kirkland: ($4.4M) PAA: 6.4M Total City: 1.9M
Low Development PAAs, Property-Tax Focused	**High** Same as baseline plus the following levy limits: 2010-2015: 5.0% 2016-2025: 4.5%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (179 to 174)	**Low** City: Baseline PAA: Low	The impact of lower PAA development is higher tax rates and a lower FTE demand overall, though the PAA fiscal impact remains positive and the taxes lower than a no annexation scenario.		Current Kirkland: ($1.8M) PAA: 2.2M Total City: .4M
High Development Current City, Property-Tax Focused	**Low** Same as baseline plus the following levy limits: 2010-2015: 3.0%	**Medium** Reduce rate of hiring: hired 7 fewer FTEs (192 to 185)	**High** City: High PAA: Baseline	The impact of high development in current Kirkland is a much lower tax need. The impact of annexation remains positive, but to a much lower degree, since most of the funding gap is solved by development in current Kirkland.		Current Kirkland: ($2.9M) PAA: 1.9M Total City: 1.0M

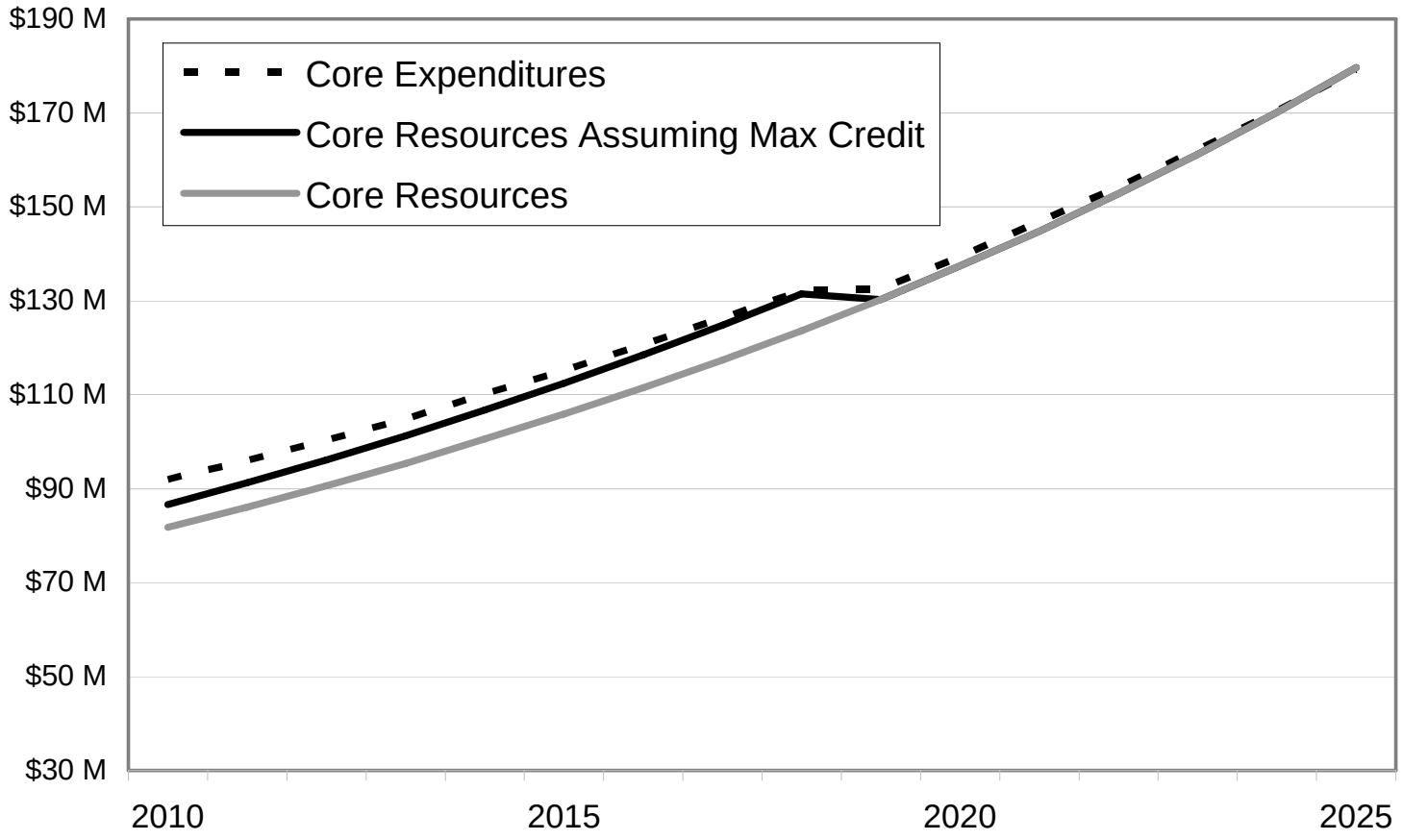
* Additional information is included in the supplemental packet.

Scenario Options

- The scenarios shown in the matrix are based on:
  - Closing the gap to within 1% of expenditures by 2020
  - A variety of combinations of the tools were tested, but those which didn't close the gap were excluded
- All strategies shown are more effective with annexation
- Different strategies perform better with addition of the PAA

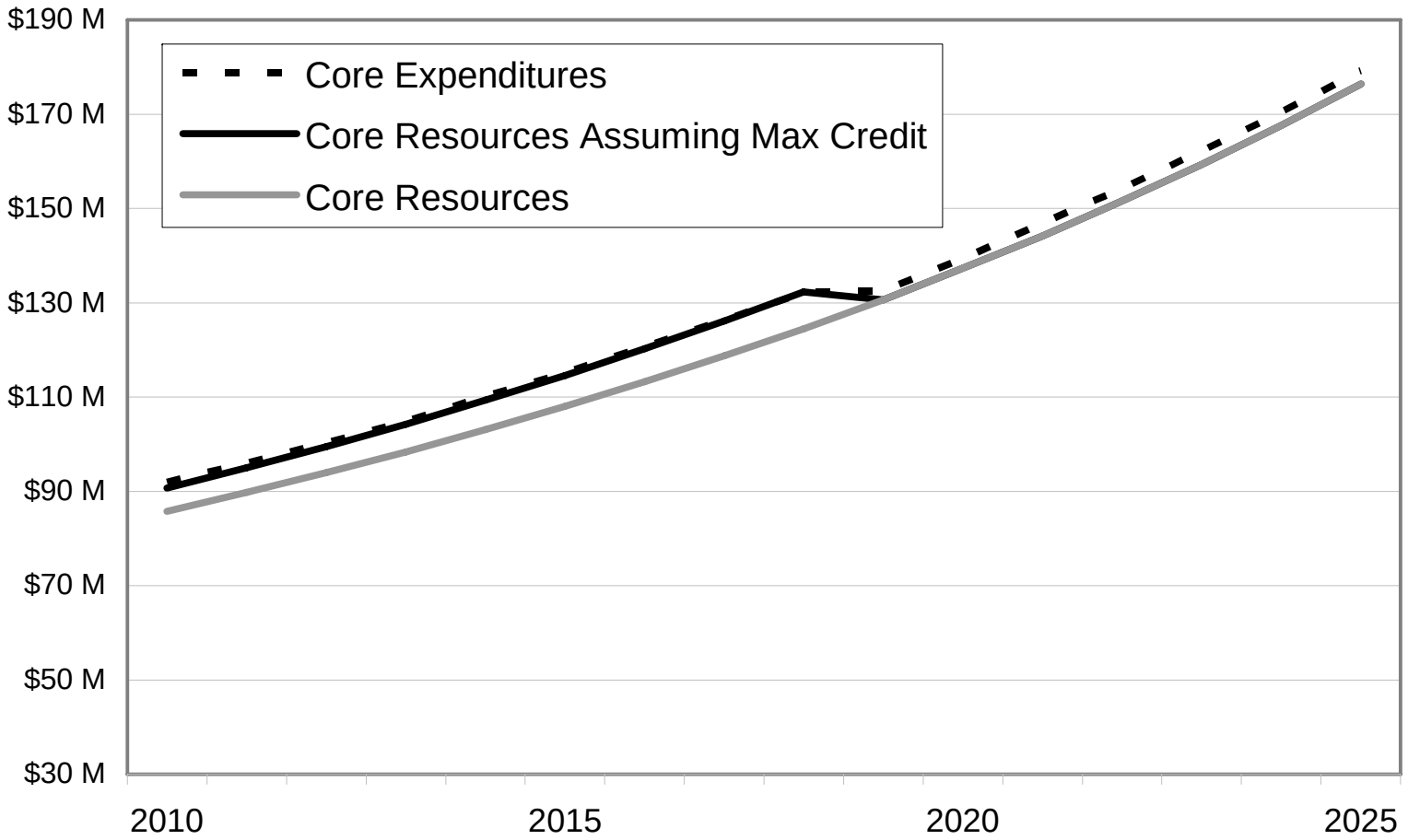
Scenario: Property Tax Focused

Tax Policies	Expenditure Management Policies	Development
High	**Medium**	**Medium**
Same as baseline plus the following levy limits: 2010-2015: 4.0% 2016-2025: 3.5%	Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	City: Baseline PAA: Baseline



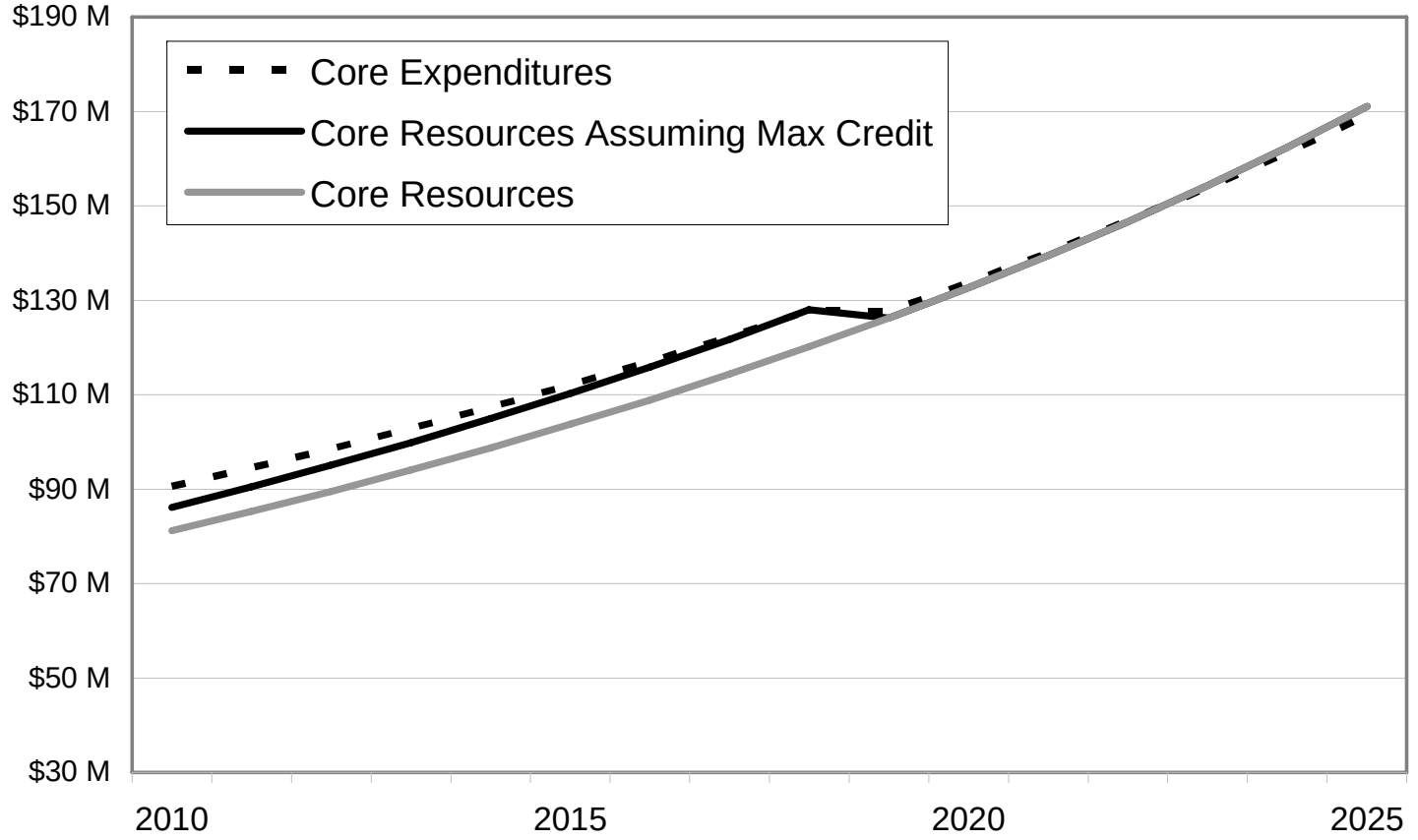
Scenario: Business Tax Focused

Tax Policies	Expenditure Management Policies	Development
High	**Medium**	**Medium**
Same as baseline plus a new business tax on gross receipts at 0.0975%	Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	City: Baseline PAA: Baseline



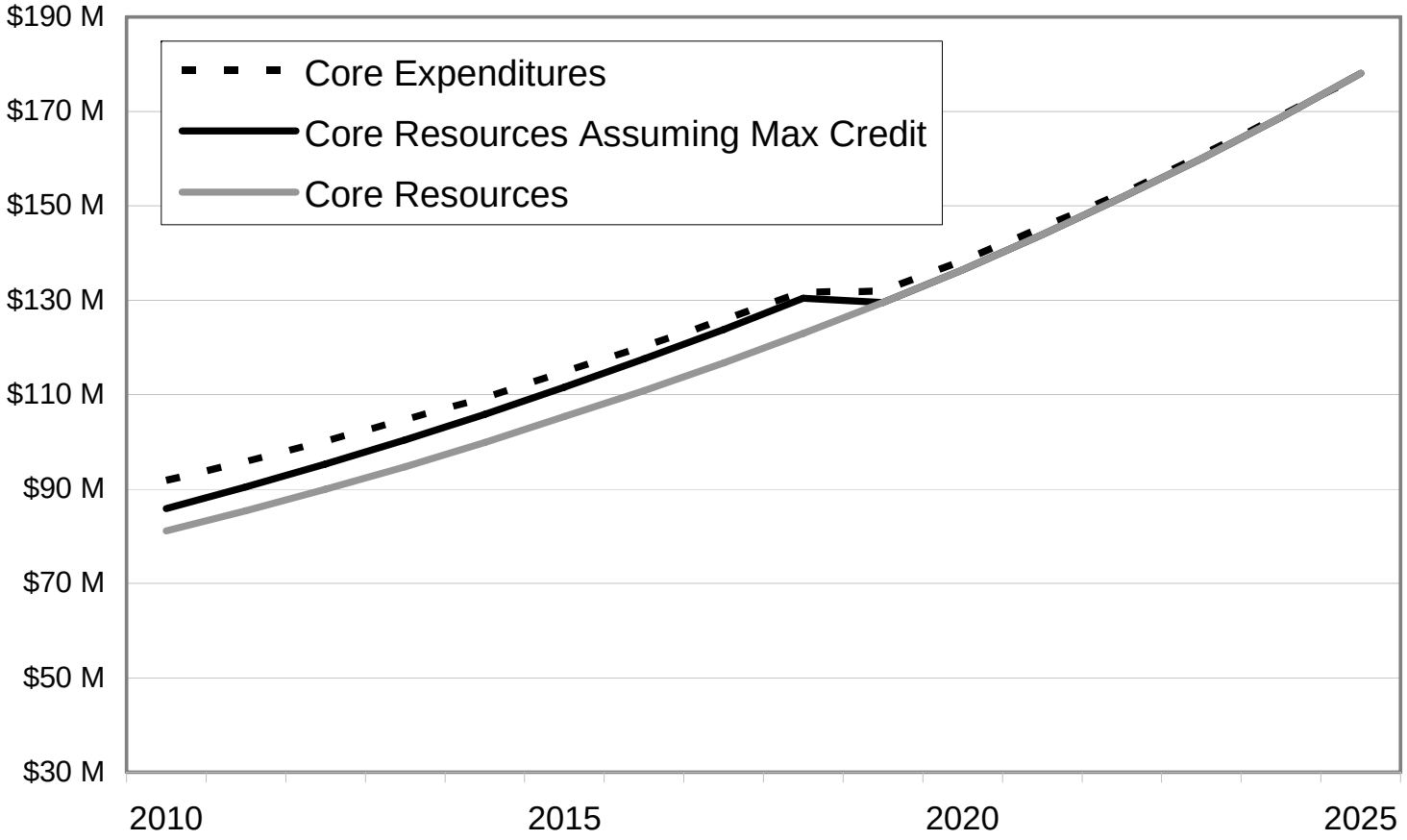
Scenario: No Growth-Related Hiring, Balance With Property Tax

Tax Policies	Expenditure Management Policies	Development
Medium	**High**	**Medium**
Same as baseline plus the following levy limits: 2010-2015: 3.0% 2016-2025: 2.5%	Reduce rate of hiring: hired 47 fewer FTEs (185 to 138)	City: Baseline PAA: Baseline



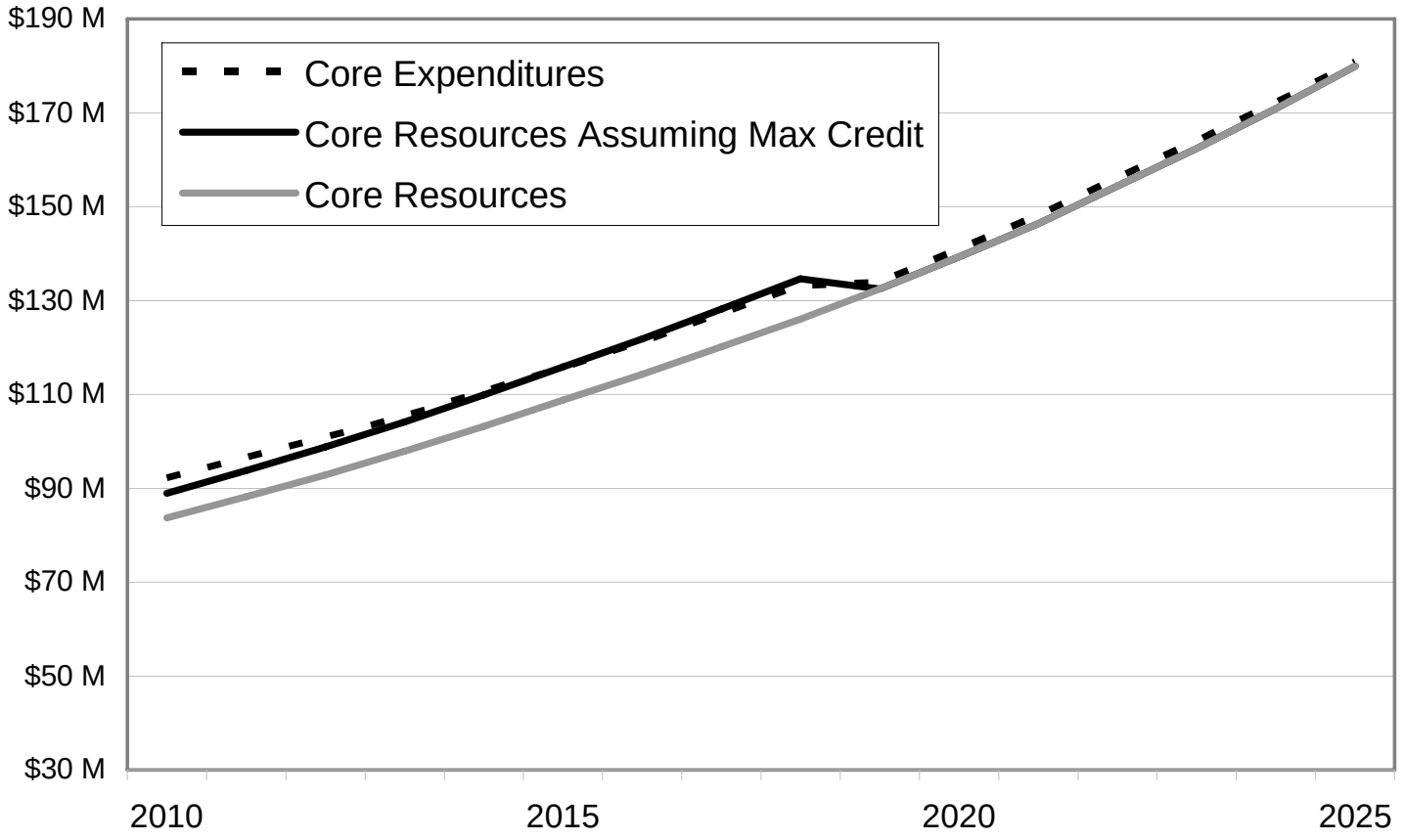
Scenario: Low Development PAAs, Property-Tax Focused

Tax Policies	Expenditure Management Policies	Development
High	**Medium**	**Low**
Same as baseline plus the following levy limits: 2010-2015: 5.0% 2016-2025: 4.5%	Reduce rate of hiring: hired 5 fewer FTEs (179 to 174)	City: Baseline PAA: Low



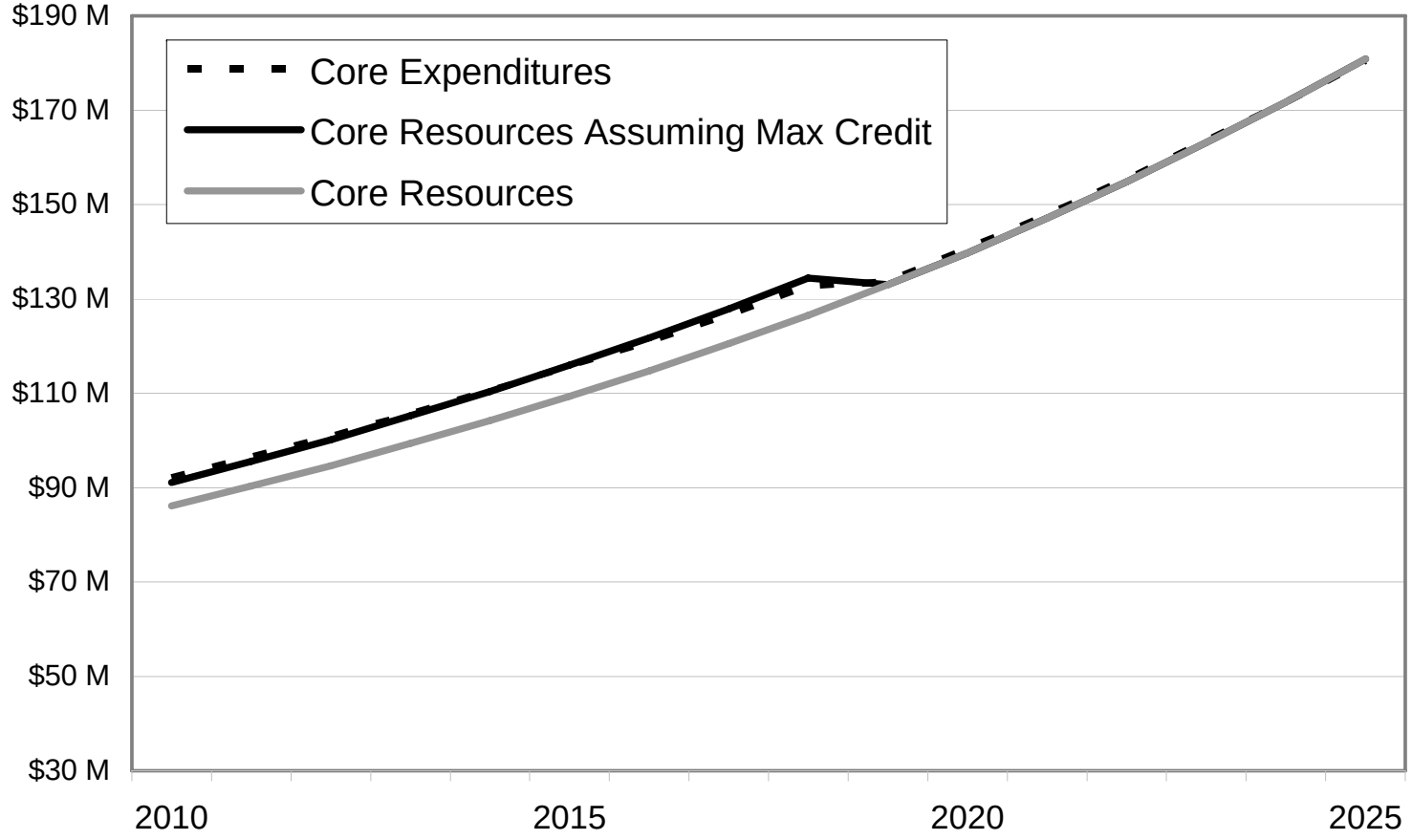
Scenario: High Development Current City, Property-Tax Focused

Tax Policies	Expenditure Management Policies	Development
Low	**Medium**	**High**
Same as baseline plus the following levy limits: 2010-2015: 3.0%	Reduce rate of hiring: hired 7 fewer FTEs (192 to 185)	City: High PAA: Baseline



Scenario: Blended Tax Scenario, Property, Business, and Utility Tax Increases

Tax Policies	Expenditure Management Policies	Development
High	**Low**	**Medium**
Levy limits of 2.0% from 2010-2025 Tax on gross receipts at 0.05% Private utility taxes at 7.5%	Hiring rate reflects current policies	City: Baseline PAA: Baseline

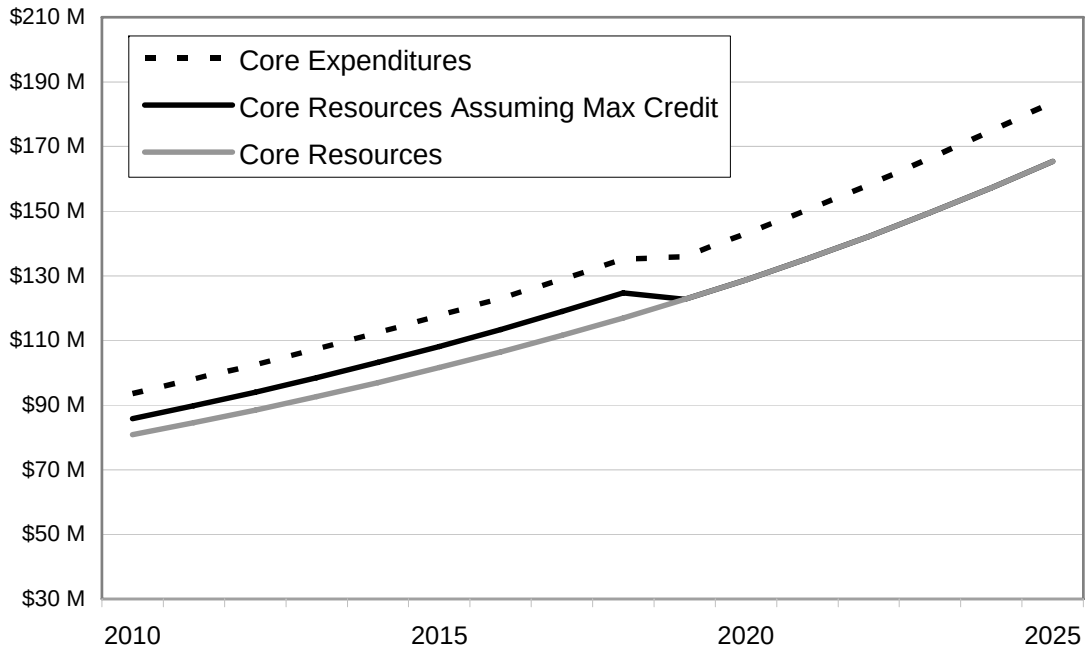


What Variables Matter?

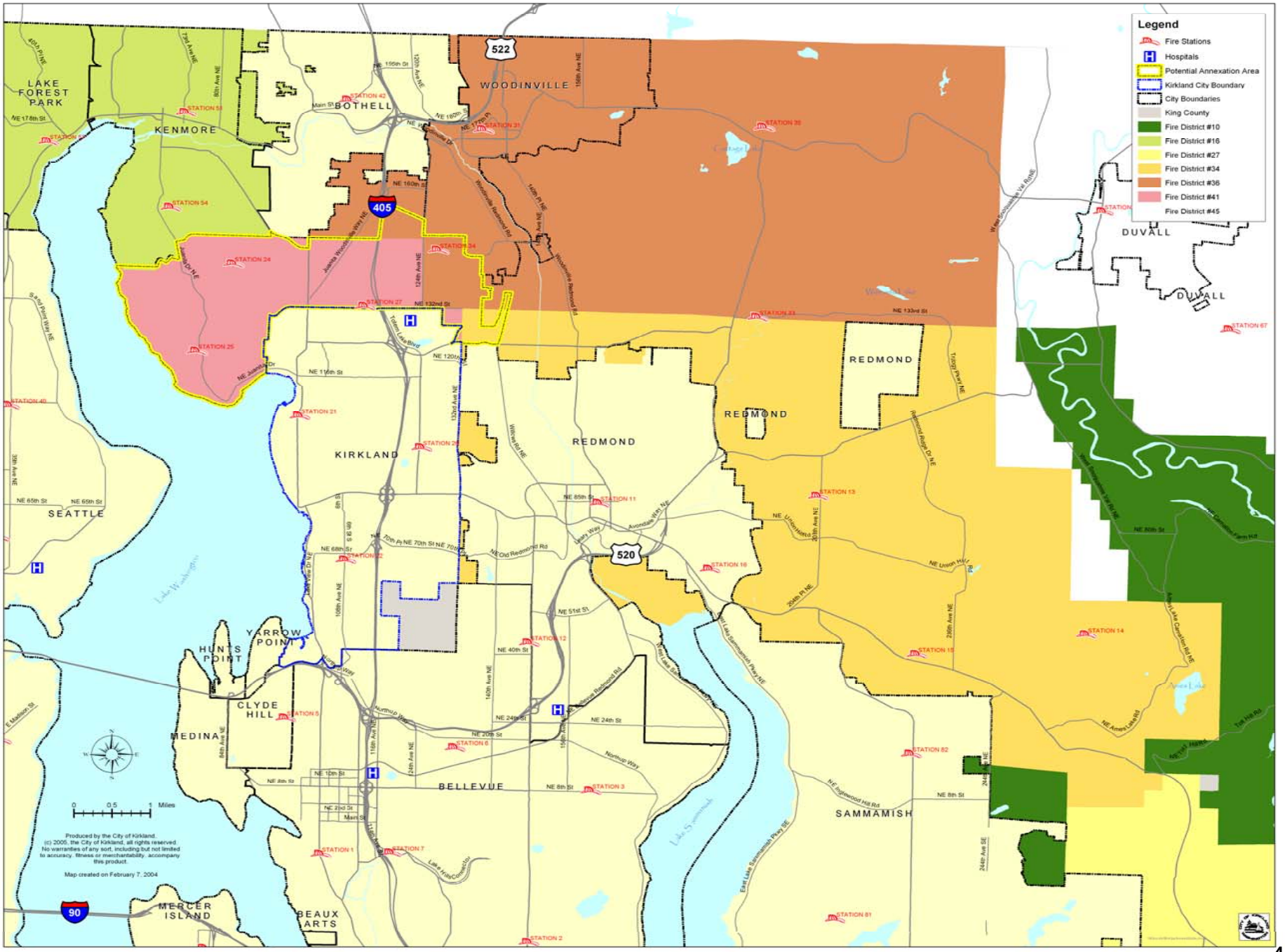
- Added costs in the PAA (example: Kingsgate Fire Station)

Scenario: Baseline With Annexation,
With Staffed Kingsgate Fire Station

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	City: Baseline PAA: Baseline



2025 Deficit
Before: $15 million
After: $18 million

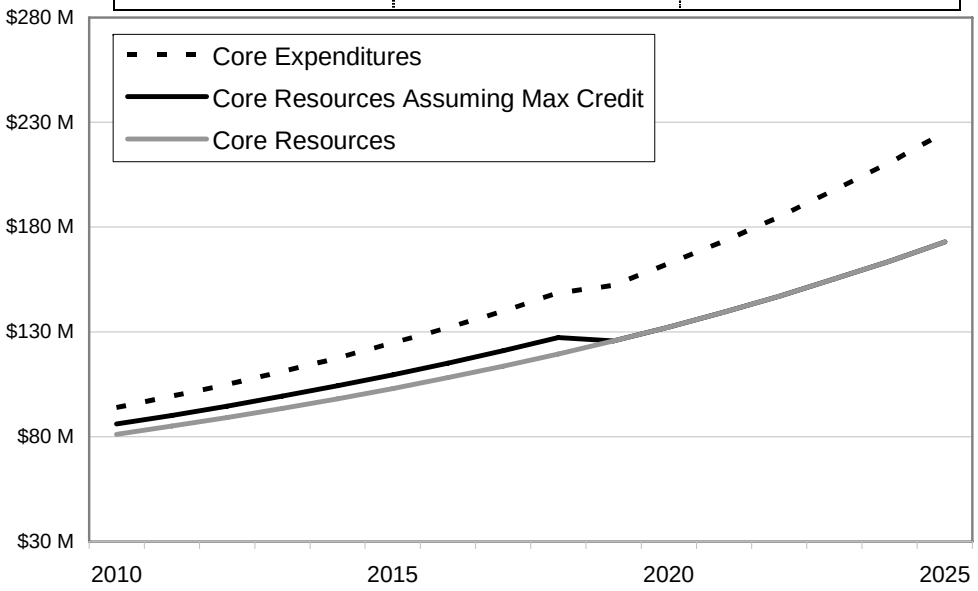

Legend
Fire Stations
Hospitals
Potential Annexation Area
Kirkland City Boundary
City Boundaries
King County
Fire District #10
Fire District #16
Fire District #27
Fire District #34
Fire District #36
Fire District #41
Fire District #45
LAKE FOREST PARK
KENMORE
BOTHELL
WOODINVILLE
DUVALL
REDMOND
KIRKLAND
SEATTLE
YARROW POINT
HUNTS POINT
CLYDE HILL
MEDINA
BELLEVUE
SAMMAMISH
MERCER ISLAND
BEAUX ARTS
522
405
520
90
0 0.5 1 Miles
Produced by the City of Kirkland.
(c) 2005, the City of Kirkland, all rights reserved.
No warranties of any sort, including but not limited to accuracy, fitness or merchantability, accompany this product.
Map created on February 7, 2004

What Variables Matter (continued)?

- The compound rate of wage and benefit inflation

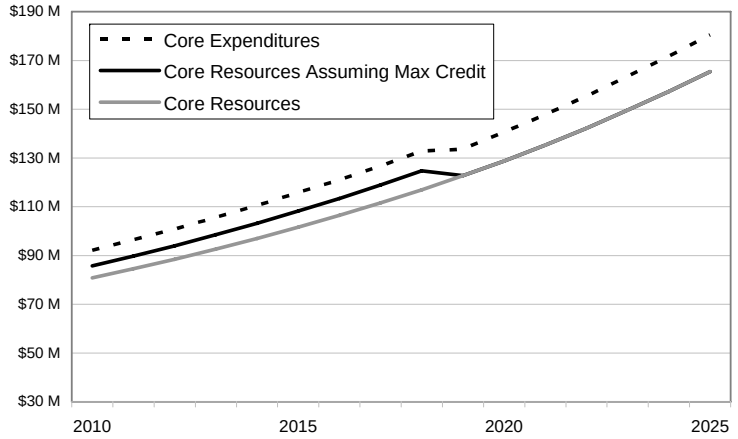
Scenario: Baseline With Annexation,
With 6% Wage Inflation, 10% Benefit Inflation

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	City: Baseline PAA: Baseline



Scenario: Baseline With Annexation

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	City: Baseline PAA: Baseline



What Variables Matter (continued)?

- In all cases:
  - A change in policy increasing revenues is required (regardless of annexation)
  - Expenditure management is less impacted by the number of FTEs added than by the wage and benefit inflation rates
  - The City cannot control the pace of development; as a result, the high scenario may not be realistic

Recap of Phase II Open Financial Issues

- Stability of state sales tax credit and method
- Infrastructure needs of the PAA
- Availability of funds from King County
- Impacts of adding fire staffing if the Kingsgate Fire station is relocated
- The ultimate sizing and configuration of the new Public Safety/Jail facilities
- Assumption that Northshore Utility District will continue to provide service, but that the franchise fee will keep pace with City utility tax rate

Objectives Revisited

- Provide responses to specific questions and requests from December 12, 2006 Study Session
- Provide a basis for discussion of policy tools and scenarios
- Provide Council with sufficient financial information to enable a decision on whether to proceed to Phase 2 of the annexation evaluation

Proposed Next Steps

- January/February — Kirkland Outreach/Financial Information
- February — Public Forum
- March — Go/No Go Decision to Proceed to Phase Two

Public Outreach

- Council Request in November to extend public outreach to Kirkland residents
  - Present results of financial analysis
  - Ask for further concerns or questions
- Staff worked with EnviroIssues to design additional outreach activities
- Two options presented
  - Focus Groups
  - Community Workshop and Forum (recommended format)

Recommended Pre-Forum Activities

- Develop updated materials for public information and an invitation to forum
- Send invitation to all who participated in prior session, listserv subscribers and key stakeholder groups (e.g. neighborhood associations, Chamber of Commerce, etc.)

Meeting Format

- Open house workshop to share information and demonstrate model to interested participations
- Staff presentation of financial analysis findings and answers to FAQ's
- Public comment period in town hall format facilitated by consultant
- Closing comments from Council

Next Steps

- Poll Council for possible dates
- Obtain facility
- Develop updated materials and invitation
- Contact stakeholders

Annexation Study Session
January 9, 2007

Supplemental Materials

Past Strategies to Address the "Diverging Lines"

Strategy	< 1999	1999	2000	2001	2002	2003	2004	2005-06
New revenue source:								
Surface water management fee	X							X
Revenue generating regulatory license fee						X		
Surface water utility tax					X			
Cost of service interfund charge	X							
Increased tax rate or fee:								
Increased property tax rate	X		X			X	X	X
Increased utility tax rate						X		X
Increased parking fines			X		X			
Increased development fees		X	X		X			
Changes to sales tax:								
Reduced CIP allocation			X					
Reduced sales tax lag to 1 year								X
Used one-time revenue source:								
Sales tax audit proceeds							X	
Interest income								X
Planned use of Rainy Day reserve						X	X	X
Expenditure reductions					X	X	X	
Other strategies:								
Used new construction growth	X	X						
Reduced budgeted benefit rate to citywide average					X			X
Reduction in state retirement rates					X			

Major Events

Revenue Impacts

- **1999**: Passage of Initiative 695 (repealing motor vehicle excise tax and requiring voter-approval of all tax and fee increases). Estimated loss of $660,000 per year. Later declared unconstitutional, but legislature subsequently approved a measure to reduce vehicle license fees
- **2000:** Passage of 722 limiting property tax increases to 2%; later ruled unconstitutional.
- **2001**: Passage of Initiative 747 limits property tax increase to 1% as of 2002.
- **2002:** General economic downturn begins mid-2002; also loss of Home Base, Apple Computer and Kirkland Nissan.
- **2002**: Initiative 776 ($30 car tabs) passed by voters. Ruled unconstitutional by Superior Court in 2003, but upheld by the State Supreme Court in 2004. Estimated annual loss of $400,000 for CIP moved planned projects to unfunded.
- **2004**: Sidewalk fee-in-lieu elimination removed $2.98 M in 6-year CIP for planned sidewalks.

Expenditure Impacts

- Added staff between 1997 and 2007 averaging 13 FTE's per year addressing service level needs (e.g., public safety, development services, and technology) and adding programs such as economic development and neighborhood traffic control.
- Health-care related benefit premiums have essentially doubled since 1998.

Development Scenario Characteristics – Average*

Development Scenarios and Outputs (AVERAGE PER YEAR)

	Current City			PAAs			Total City		
	Low	Baseline	High	Low	Baseline	High	Low	Baseline	High
Residential									
SF DU Developed/Year	117	171	255	64	103	139	181	273	394
Net SF DU Added/Year	77	97	97	53	84	111	130	181	208
MF DU Developed/Year	159	206	232	77	125	161	236	331	393
Net MF DU Added/Year	135	171	174	68	110	143	203	281	317
Commercial									
Net Sq Ft Added (Retail)/Year	55,661	54,299	124,941	16,558	27,533	43,479	72,219	81,831	168,419
Net Sq Ft Added (Non-retail)/Year	14,792	100,840	143,454	22,927	36,867	57,212	37,719	137,707	200,667
Net Sq Ft Added (Total)/Year	70,453	155,139	268,395	39,485	64,399	100,691	109,938	219,538	369,086

SF DU – Single Family Dwelling Unit

MF DU – Multi-Family Dwelling Unit

* Additional information is included in the supplemental packet.

Development Scenario Characteristics – Total*

Development Scenarios and Outputs (TOTAL)

	Current City			PAAs			Total City		
	Low	Baseline	High	Low	Baseline	High	Low	Baseline	High
Residential									
SF DU Developed	2,338	3,413	5,106	1,282	2,055	2,775	3,620	5,468	7,881
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Net Sq Ft Added (Non-retail)	295,835	1,396,753	2,869,090	458,540	737,334	1,144,243	754,376	2,754,136	4,013,333
Net Sq Ft Added (Total)	1,409,053	3,102,772	5,367,906	789,702	1,287,988	2,013,814	2,198,755	4,390,760	7,381,720
% AV from New Construction	1.26%	1.70%	2.22%	1.44%	2.16%	2.74%	1.31%	1.84%	2.38%

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	Tools			Long-Term Fiscal Outlook		
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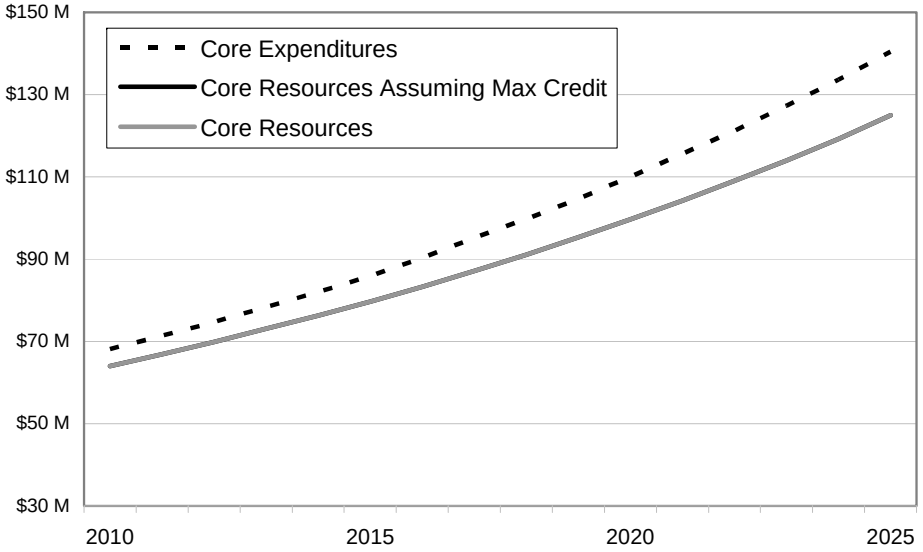
Baseline No Annexation	No change in tax policy 1% property tax limit	Hiring rate reflects current policies	Baseline	**O&M Impacts** Deficits in all years Deficit grows to $15.5M by 2025 Def. as % of exp.: 1% to 11% Cost growth: 5.1%/yr Revenue growth: 4.5%/yr	**Facilities** $30 M unfunded need Annual D/S: $2.3 M	**Surplus/Deficit in 2025** Current Kirkland: ($15.5M) PAA: 0.0M Total City: (15.5M)
Annexation Scenarios						
Baseline With Annexation	Same as above	Same as above	City: Baseline PAA: Baseline	**O&M Impacts** Citywide deficit marginally reduced PAA deficit starts at 15% and ends at 1% Cost growth:6.4%/yr Revenue growth: 6.0%/yr	**Facilities** $80 M need citywide $38 M impact from annexation 30-year bond -- $3.3M/yr (all city) 10-year bond -- $5.9M/yr (PAA impact)	**Surplus/Deficit in 2025** Current Kirkland: ($14.8M) PAA: (0.3M) Total City: (15.1M)
Balanced Scenarios (closes fiscal gap to within 1% of Expenditures in 2020)						
Property-Tax Focused	**High** Same as baseline plus the following levy limits: 2010-2015: 4.0% 2016-2025: 3.5%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	**Medium** City: Baseline PAA: Baseline	Balancing with primarily property tax results in net gains from the annexation areas which help offset base City structural deficit issues. Without annexation, tax rates would need to be higher to achieve the same ends.		Current Kirkland: ($4.1M) PAA: 4.6M Total City: .5M
Business-Tax Focused	**High** Same as baseline plus a new business tax on gross receipts at 0.0975%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	**Medium** City: Baseline PAA: Baseline	This scenario is similar to the property tax based scenario except the net contribution from annexation is smaller, since the tax is based on busineses only.		Current Kirkland: ($5.7M) PAA: 2.9M Total City: (2.8M)
No Growth-Related Hiring, Balance With Property Tax	**Medium** Same as baseline plus the following levy limits: 2010-2015: 3.0% 2016-2025: 2.5%	**High** Reduce rate of hiring: hired 47 fewer FTEs (185 to 138)	**Medium** City: Baseline PAA: Baseline	The impact of much lower hiring reduces the need for new taxes, though at a likely cost in terms of level-of-service. The impact of annexation is even more positive as the rate of growth in the annexation areas is somewhat higher than current Kirkland.		Current Kirkland: ($4.4M) PAA: 6.4M Total City: 1.9M
Low Development PAAs, Property-Tax Focused	**High** Same as baseline plus the following levy limits: 2010-2015: 5.0% 2016-2025: 4.5%	**Medium** Reduce rate of hiring: hired 5 fewer FTEs (179 to 174)	**Low** City: Baseline PAA: Low	The impact of lower PAA development is higher tax rates and a lower FTE demand overall, though the PAA fiscal impact remains positive and the taxes lower than a no annexation scenario.		Current Kirkland: ($1.8M) PAA: 2.2M Total City: .4M
High Development Current City, Property-Tax Focused	**Low** Same as baseline plus the following levy limits: 2010-2015: 3.0%	**Medium** Reduce rate of hiring: hired 7 fewer FTEs (192 to 185)	**High** City: High PAA: Baseline	The impact of high development in current Kirkland is a much lower tax need. The impact of annexation remains positive, but to a much lower degree, since most of the funding gap is solved by development in current Kirkland.		Current Kirkland: ($2.9M) PAA: 1.9M Total City: 1.0M

Scenario: Baseline No Annexation

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	Baseline



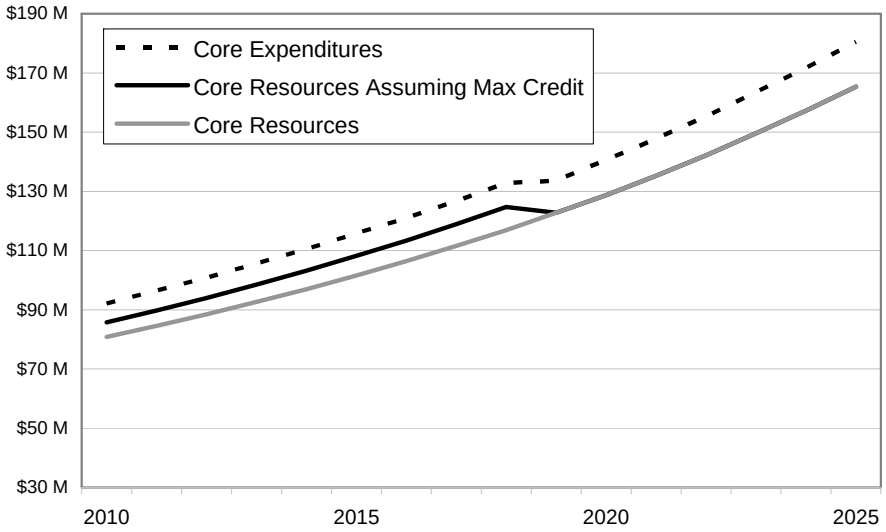
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,804	83,604	107,673	138,105
Facility Debt Service (000's)	2,295	2,295	2,295	2,295
Subtotal Expenditures	**68,099**	**85,899**	**109,968**	**140,400**
Core Resources (000's)	64,000	79,685	99,650	124,937
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,000**	**79,685**	**99,650**	**124,937**
Net Resources (000's)	**(4,099)**	**(6,214)**	**(10,318)**	**(15,462)**
Deficit as % of Expenditures	**-6%**	**-7%**	**-10%**	**-11%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	0	0	0	0
Facility Debt Service (000's)	0	0	0	0
Subtotal Expenditures	**0**	**0**	**0**	**0**
Core Resources (000's)	0	0	0	0
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**0**	**0**	**0**	**0**
Net Resources (000's)	**0**	**0**	**0**	**0**
Deficit as % of Expenditures	**N/A**	**N/A**	**N/A**	**N/A**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	65,804	83,604	107,673	138,105
Facility Debt Service (000's)	2,295	2,295	2,295	2,295
Subtotal Expenditures	**68,099**	**85,899**	**109,968**	**140,400**
Core Resources (000's)	64,000	79,685	99,650	124,937
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,000**	**79,685**	**99,650**	**124,937**
Net Resources (000's)	**(4,099)**	**(6,214)**	**(10,318)**	**(15,462)**
Deficit as % of Core Expenditures	**-6%**	**-7%**	**-10%**	**-11%**

Scenario: Baseline With Annexation

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	City: Baseline PAA: Baseline



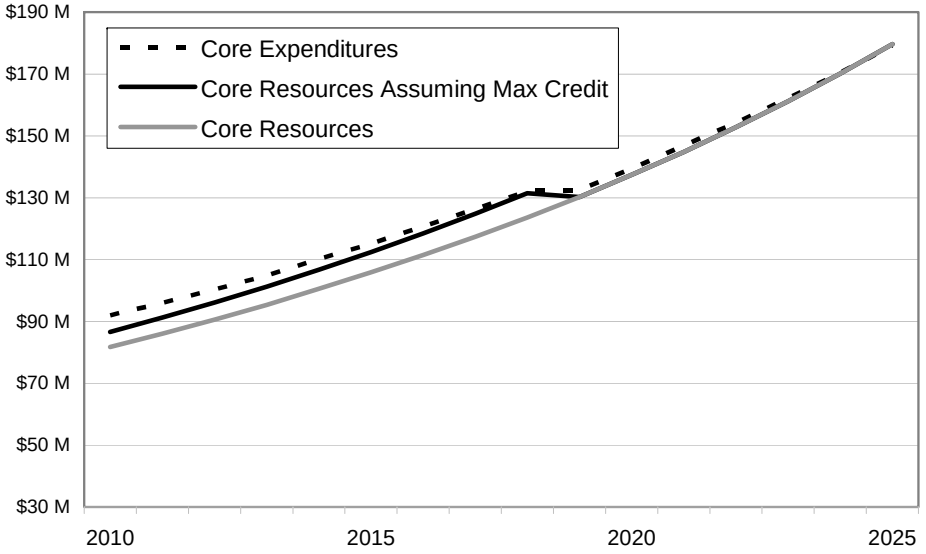
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,843	83,819	107,752	138,083
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**68,153**	**86,129**	**110,042**	**140,330**
Core Resources (000's)	64,326	80,067	100,110	125,510
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,326**	**80,067**	**100,110**	**125,510**
Net Resources (000's)	**(3,827)**	**(6,062)**	**(9,932)**	**(14,820)**
Deficit as % of Expenditures	**-6%**	**-7%**	**-9%**	**-11%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,079	22,751	29,565	39,117
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**23,953**	**29,624**	**30,587**	**40,181**
Core Resources (000's)	16,507	21,557	28,618	39,902
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**21,433**	**28,123**	**28,618**	**39,902**
Net Resources (000's)	**(2,520)**	**(1,502)**	**(1,969)**	**(279)**
Deficit as % of Expenditures	**-15%**	**-7%**	**-7%**	**-1%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,922	106,569	137,317	177,200
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**92,106**	**115,753**	**140,628**	**180,511**
Core Resources (000's)	80,833	101,624	128,727	165,412
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**85,759**	**108,190**	**128,727**	**165,412**
Net Resources (000's)	**(6,347)**	**(7,564)**	**(11,901)**	**(15,099)**
Deficit as % of Core Expenditures	**-8%**	**-7%**	**-9%**	**-9%**

Scenario: Property Tax Focused

Tax Policies	Expenditure Management Policies	Development
High	**Medium**	**Medium**
Same as baseline plus the following levy limits: 2010-2015: 4.0% 2016-2025: 3.5%	Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	City: Baseline PAA: Baseline



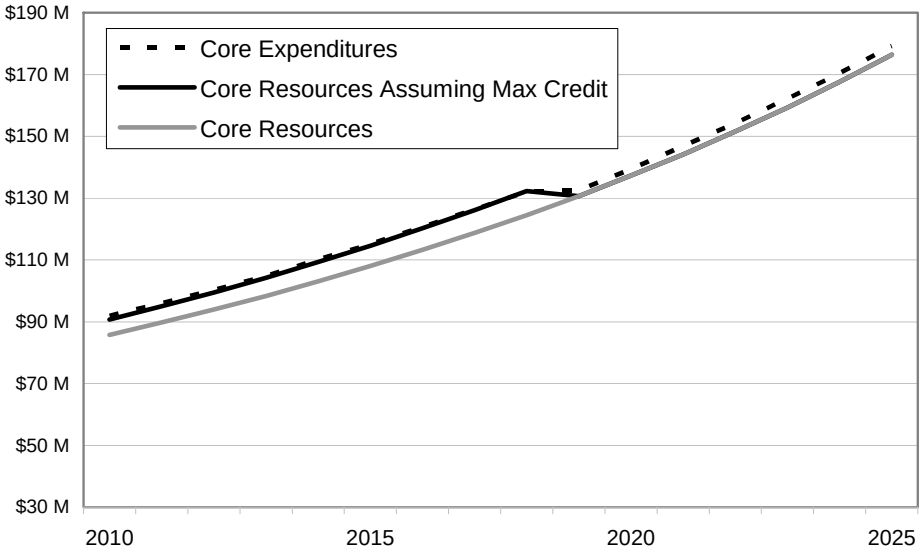
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,681	83,578	106,710	137,171
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**67,992**	**85,888**	**109,000**	**139,419**
Core Resources (000's)	64,955	83,135	105,947	135,277
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,955**	**83,135**	**105,947**	**135,277**
Net Resources (000's)	**(3,037)**	**(2,753)**	**(3,053)**	**(4,142)**
Deficit as % of Expenditures	**-5%**	**-3%**	**-3%**	**-3%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,048	22,390	29,270	38,677
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**23,921**	**29,264**	**30,292**	**39,741**
Core Resources (000's)	16,747	22,750	31,445	44,361
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**21,674**	**29,315**	**31,445**	**44,361**
Net Resources (000's)	**(2,248)**	**51**	**1,153**	**4,619**
Deficit as % of Expenditures	**-13%**	**0%**	**4%**	**12%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,729	105,968	135,980	175,848
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**91,913**	**115,152**	**139,291**	**179,160**
Core Resources (000's)	81,702	105,885	137,391	179,637
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**86,629**	**112,450**	**137,391**	**179,637**
Net Resources (000's)	**(5,284)**	**(2,702)**	**(1,900)**	**477**
Deficit as % of Core Expenditures	**-6%**	**-3%**	**-1%**	**0%**

Scenario: Business Tax Focused

Tax Policies	Expenditure Management Policies	Development
High	**Medium**	**Medium**
Same as baseline plus a new business tax on gross receipts at 0.0975%	Reduce rate of hiring: hired 5 fewer FTEs (185 to 180)	City: Baseline PAA: Baseline



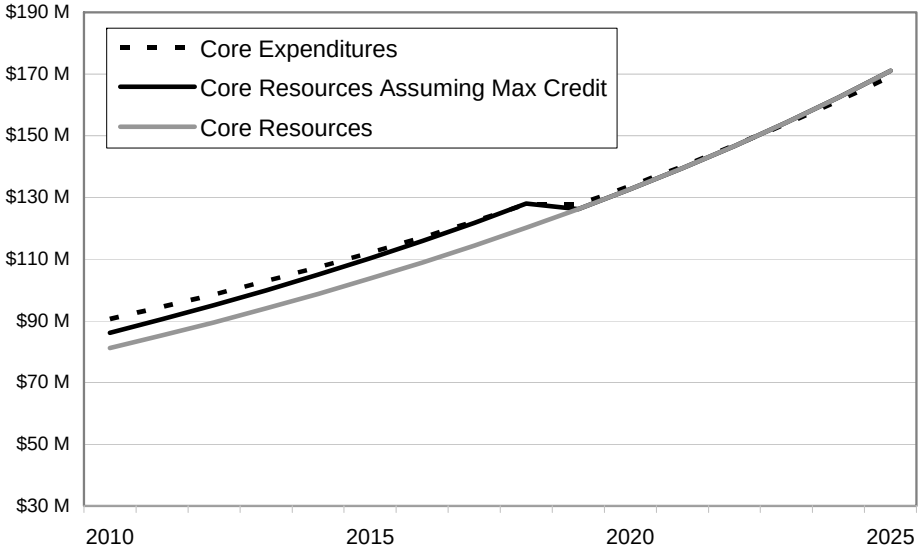
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,681	83,578	106,710	137,171
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**67,992**	**85,888**	**109,000**	**139,419**
Core Resources (000's)	68,463	85,381	106,677	133,750
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**68,463**	**85,381**	**106,677**	**133,750**
Net Resources (000's)	**471**	**(507)**	**(2,323)**	**(5,668)**
Deficit as % of Expenditures	**1%**	**-1%**	**-2%**	**-4%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,048	22,390	29,270	38,677
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**23,921**	**29,264**	**30,292**	**39,741**
Core Resources (000's)	17,283	22,630	30,631	42,600
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**22,209**	**29,195**	**30,631**	**42,600**
Net Resources (000's)	**(1,712)**	**(69)**	**340**	**2,859**
Deficit as % of Expenditures	**-10%**	**0%**	**1%**	**7%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,729	105,968	135,980	175,848
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**91,913**	**115,152**	**139,291**	**179,160**
Core Resources (000's)	85,746	108,011	137,309	176,350
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**90,672**	**114,577**	**137,309**	**176,350**
Net Resources (000's)	**(1,241)**	**(575)**	**(1,983)**	**(2,810)**
Deficit as % of Core Expenditures	**-2%**	**-1%**	**-1%**	**-2%**

Scenario: No Growth-Related Hiring, Balance With Property Tax

Tax Policies	Expenditure Management Policies	Development
Medium	**High**	**Medium**
Same as baseline plus the following levy limits: 2010-2015: 3.0% 2016-2025: 2.5%	Reduce rate of hiring: hired 47 fewer FTEs (185 to 138)	City: Baseline PAA: Baseline



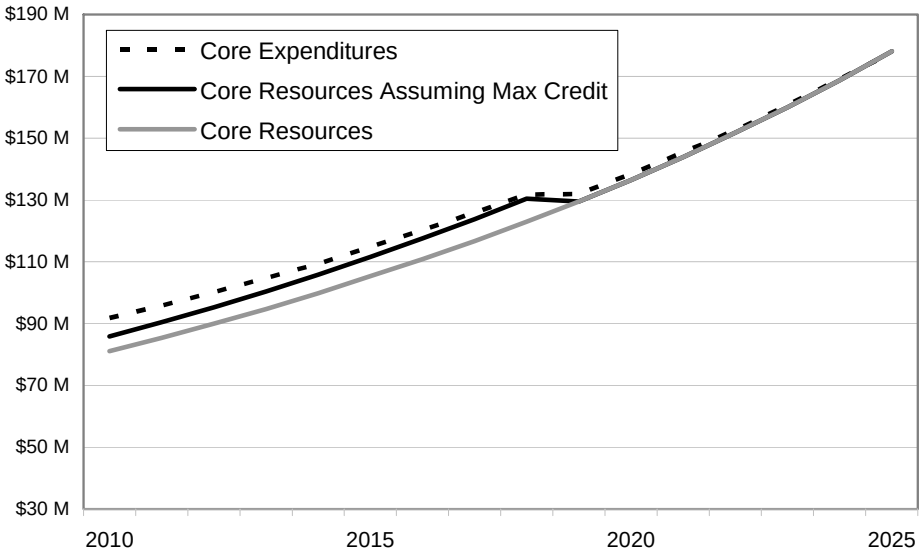
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	64,679	81,652	103,507	131,746
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**66,990**	**83,962**	**105,797**	**133,993**
Core Resources (000's)	64,551	81,607	102,738	129,553
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,551**	**81,607**	**102,738**	**129,553**
Net Resources (000's)	**(2,439)**	**(2,355)**	**(3,059)**	**(4,440)**
Deficit as % of Expenditures	**-4%**	**-3%**	**-3%**	**-3%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	16,787	21,218	26,865	34,069
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**23,660**	**28,092**	**27,887**	**35,133**
Core Resources (000's)	16,658	22,154	29,908	41,501
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**21,585**	**28,719**	**29,908**	**41,501**
Net Resources (000's)	**(2,075)**	**627**	**2,022**	**6,368**
Deficit as % of Expenditures	**-12%**	**3%**	**8%**	**19%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	81,466	102,870	130,372	165,815
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**90,650**	**112,054**	**133,684**	**169,126**
Core Resources (000's)	81,209	103,761	132,646	171,054
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**86,135**	**110,326**	**132,646**	**171,054**
Net Resources (000's)	**(4,514)**	**(1,728)**	**(1,038)**	**1,928**
Deficit as % of Core Expenditures	**-6%**	**-2%**	**-1%**	**1%**

Scenario: Low Development PAAs, Property-Tax Focused

Tax Policies	Expenditure Management Policies	Development
High	**Medium**	**Low**
Same as baseline plus the following levy limits: 2010-2015: 5.0% 2016-2025: 4.5%	Reduce rate of hiring: hired 5 fewer FTEs (179 to 174)	City: Baseline PAA: Low



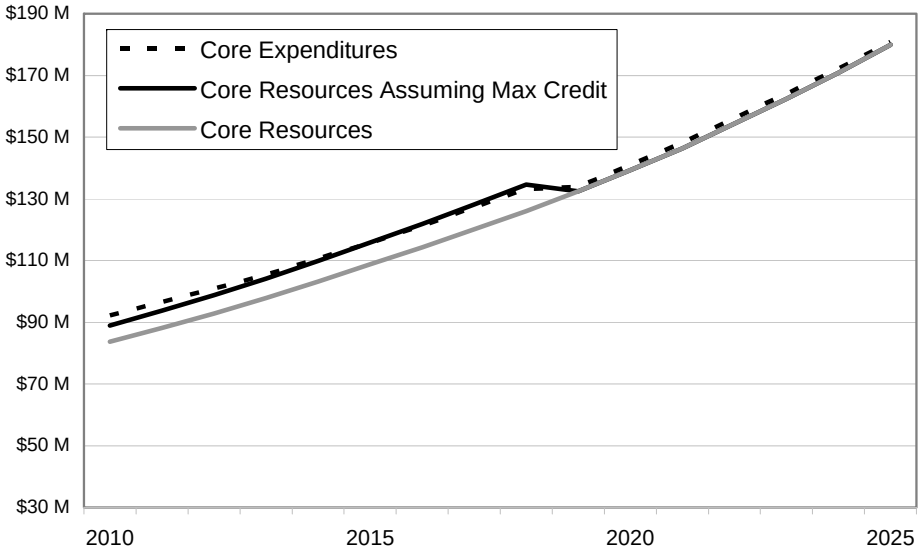
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,690	83,597	106,718	137,247
Facility Debt Service (000's)	2,327	2,346	2,349	2,336
Subtotal Expenditures	**68,017**	**85,942**	**109,068**	**139,583**
Core Resources (000's)	64,853	83,571	107,231	137,800
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,853**	**83,571**	**107,231**	**137,800**
Net Resources (000's)	**(3,164)**	**(2,371)**	**(1,836)**	**(1,783)**
Deficit as % of Expenditures	**-5%**	**-3%**	**-2%**	**-1%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	16,976	22,022	28,339	37,122
Facility Debt Service (000's)	6,857	6,838	962	976
Subtotal Expenditures	**23,833**	**28,860**	**29,302**	**38,098**
Core Resources (000's)	16,207	21,741	29,153	40,294
State Sales Tax Credit ('000's)	4,817	6,317	0	0
Subtotal Revenues	**21,024**	**28,058**	**29,153**	**40,294**
Net Resources (000's)	**(2,809)**	**(802)**	**(148)**	**2,196**
Deficit as % of Expenditures	**-17%**	**-4%**	**-1%**	**6%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,666	105,618	135,057	174,370
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**91,850**	**114,802**	**138,369**	**177,681**
Core Resources (000's)	81,060	105,312	136,384	178,094
State Sales Tax Credit ('000's)	4,817	6,317	0	0
Subtotal Revenues	**85,877**	**111,628**	**136,384**	**178,094**
Net Resources (000's)	**(5,973)**	**(3,174)**	**(1,985)**	**413**
Deficit as % of Core Expenditures	**-7%**	**-3%**	**-1%**	**0%**

Scenario: High Development Current City, Property-Tax Focused

Tax Policies	Expenditure Management Policies	Development
Low	**Medium**	**High**
Same as baseline plus the following levy limits: 2010-2015: 3.0%	Reduce rate of hiring: hired 7 fewer FTEs (192 to 185)	City: High PAA: Baseline



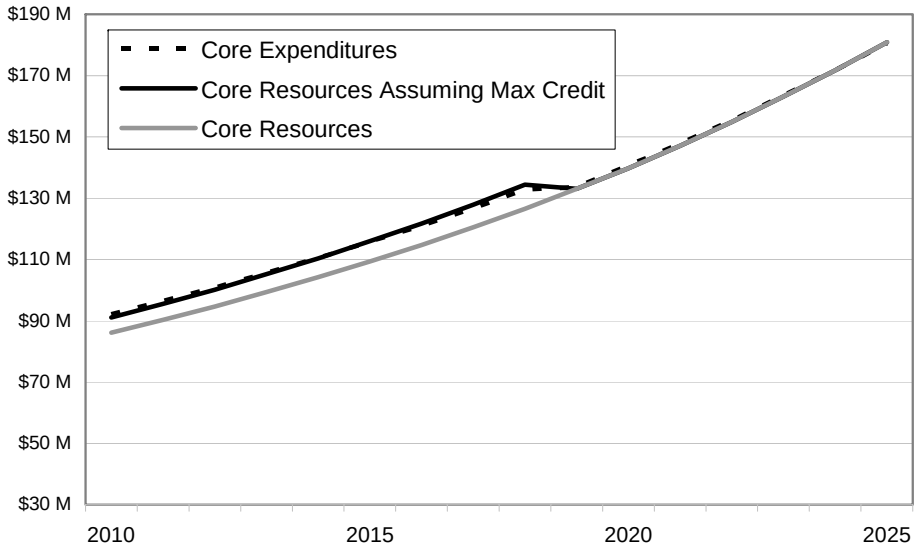
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,906	84,363	108,149	139,107
Facility Debt Service (000's)	2,326	2,341	2,334	2,304
Subtotal Expenditures	**68,232**	**86,704**	**110,483**	**141,411**
Core Resources (000's)	66,841	86,271	109,254	138,532
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**66,841**	**86,271**	**109,254**	**138,532**
Net Resources (000's)	**(1,390)**	**(434)**	**(1,229)**	**(2,880)**
Deficit as % of Expenditures	**-2%**	**-1%**	**-1%**	**-2%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,058	22,156	29,515	38,483
Facility Debt Service (000's)	6,858	6,843	977	1,007
Subtotal Expenditures	**23,916**	**28,999**	**30,493**	**39,490**
Core Resources (000's)	16,874	22,524	29,997	41,370
State Sales Tax Credit ('000's)	5,251	7,126	0	0
Subtotal Revenues	**22,125**	**29,650**	**29,997**	**41,370**
Net Resources (000's)	**(1,791)**	**651**	**(496)**	**1,879**
Deficit as % of Expenditures	**-10%**	**3%**	**-2%**	**5%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,964	106,519	137,664	177,590
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**92,148**	**115,703**	**140,975**	**180,902**
Core Resources (000's)	83,715	108,795	139,251	179,901
State Sales Tax Credit ('000's)	5,251	7,126	0	0
Subtotal Revenues	**88,966**	**115,920**	**139,251**	**179,901**
Net Resources (000's)	**(3,181)**	**217**	**(1,725)**	**(1,001)**
Deficit as % of Core Expenditures	**-4%**	**0%**	**-1%**	**-1%**

Scenario: Blended Tax Scenario, Property, Business, and Utility Tax Increases

Tax Policies	Expenditure Management Policies	Development
High	**Low**	**Medium**
Levy limits of 2.0% from 2010-2025 Tax on gross receipts at 0.05% Private utility taxes at 7.5%	Hiring rate reflects current policies	City: Baseline PAA: Baseline



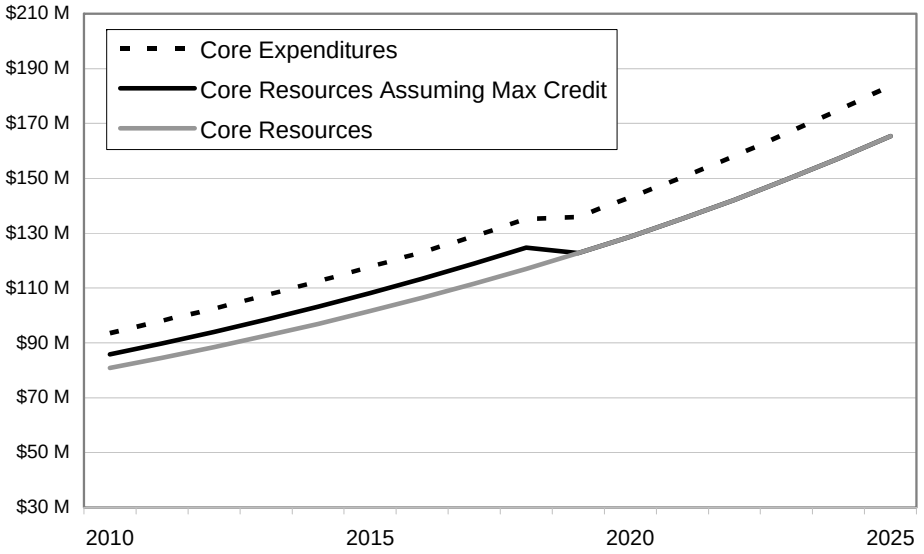
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,843	83,819	107,752	138,083
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**68,153**	**86,129**	**110,042**	**140,330**
Core Resources (000's)	68,205	85,676	107,937	136,151
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**68,205**	**85,676**	**107,937**	**136,151**
Net Resources (000's)	**52**	**(453)**	**(2,105)**	**(4,179)**
Deficit as % of Expenditures	**0%**	**-1%**	**-2%**	**-3%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,079	22,751	29,565	39,117
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**23,953**	**29,624**	**30,587**	**40,181**
Core Resources (000's)	17,917	23,714	31,850	44,739
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**22,844**	**30,279**	**31,850**	**44,739**
Net Resources (000's)	**(1,109)**	**655**	**1,263**	**4,558**
Deficit as % of Expenditures	**-6%**	**3%**	**4%**	**12%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,922	106,569	137,317	177,200
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**92,106**	**115,753**	**140,628**	**180,511**
Core Resources (000's)	86,123	109,390	139,787	180,890
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**91,049**	**115,955**	**139,787**	**180,890**
Net Resources (000's)	**(1,057)**	**202**	**(841)**	**379**
Deficit as % of Core Expenditures	**-1%**	**0%**	**-1%**	**0%**

Scenario: Baseline With Annexation, With Staffed Kingsgate Fire Station

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	City: Baseline PAA: Baseline



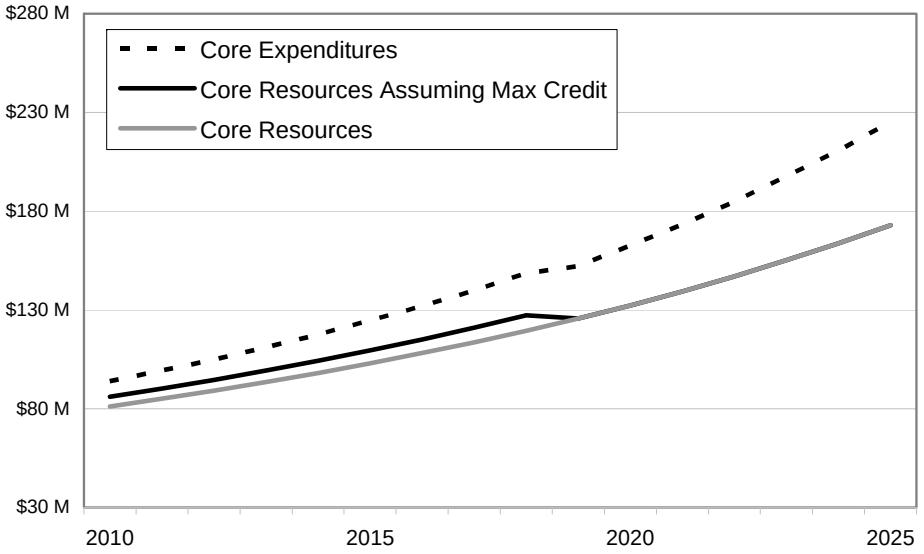
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	65,843	83,819	107,752	138,083
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**68,153**	**86,129**	**110,042**	**140,330**
Core Resources (000's)	64,326	80,067	100,110	125,510
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,326**	**80,067**	**100,110**	**125,510**
Net Resources (000's)	**(3,827)**	**(6,062)**	**(9,932)**	**(14,820)**
Deficit as % of Expenditures	**-6%**	**-7%**	**-9%**	**-11%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	18,579	24,674	32,035	42,291
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**25,452**	**31,548**	**33,057**	**43,356**
Core Resources (000's)	16,507	21,557	28,618	39,902
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**21,433**	**28,123**	**28,618**	**39,902**
Net Resources (000's)	**(4,019)**	**(3,425)**	**(4,439)**	**(3,454)**
Deficit as % of Expenditures	**-22%**	**-14%**	**-14%**	**-8%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	84,421	108,493	139,787	180,374
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**93,605**	**117,677**	**143,098**	**183,686**
Core Resources (000's)	80,833	101,624	128,727	165,412
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**85,759**	**108,190**	**128,727**	**165,412**
Net Resources (000's)	**(7,846)**	**(9,487)**	**(14,371)**	**(18,274)**
Deficit as % of Core Expenditures	**-9%**	**-9%**	**-10%**	**-10%**

Scenario: Baseline With Annexation, With 6% Wage Inflation, 10% Benefit Inflation

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies	City: Baseline PAA: Baseline



Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	67,218	90,596	124,394	171,718
Facility Debt Service (000's)	2,311	2,310	2,290	2,247
Subtotal Expenditures	**69,529**	**92,906**	**126,683**	**173,966**
Core Resources (000's)	64,527	81,074	102,642	130,753
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	**64,527**	**81,074**	**102,642**	**130,753**
Net Resources (000's)	**(5,002)**	**(11,832)**	**(24,041)**	**(43,213)**
Deficit as % of Expenditures	**-7%**	**-13%**	**-19%**	**-25%**

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,491	24,890	34,851	50,184
Facility Debt Service (000's)	6,873	6,874	1,022	1,064
Subtotal Expenditures	**24,364**	**31,764**	**35,873**	**51,248**
Core Resources (000's)	16,585	21,966	29,597	42,110
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**21,511**	**28,531**	**29,597**	**42,110**
Net Resources (000's)	**(2,853)**	**(3,233)**	**(6,276)**	**(9,138)**
Deficit as % of Expenditures	**-16%**	**-13%**	**-18%**	**-18%**

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	84,709	115,486	159,245	221,902
Facility Debt Service (000's)	9,184	9,184	3,312	3,312
Subtotal Expenditures	**93,893**	**124,670**	**162,557**	**225,214**
Core Resources (000's)	81,112	103,040	132,239	172,862
State Sales Tax Credit ('000's)	4,926	6,565	0	0
Subtotal Revenues	**86,038**	**109,605**	**132,239**	**172,862**
Net Resources (000's)	**(7,854)**	**(15,065)**	**(30,317)**	**(52,352)**
Deficit as % of Core Expenditures	**-9%**	**-13%**	**-19%**	**-24%**